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No. 340, October Term, 1929

In the Supreme Court of the United States

October Term, 1929

UNITED STATES OF AMERICA,
Petitioner,

vs.

NELSON B. UPDIKE, ET AL.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR NELSON B. UPDIKE, ET AL., RESPONDENTS

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INDEX

	Page
QUESTIONS PRESENTED	2
STATEMENT OF FACTS	3-7
SYNOPSIS OF ARGUMENT	7-16
ARGUMENT	17-158
The Bar of Section 278 (d) of the Revenue Act of 1926	17-36
The Trust Fund Theory	36-51, 129-141
The Taxpayers' Returns and the Limitations under Acts of 1921, 1924 and 1926	51-128
The Government as a Subsequent Creditor	129-141
The Liability of the Taxpayer under the Act of October 3, 1917	142-158
CONCLUSION	159

TABLE OF CASES CITED

Court Decisions

Page

Aldrich v. Vanhemert, 205 Ia. 460 140
Anderson v. Railway Co., 216 Fed. 83 16

Bank v. Braithwaite, 7 N. D. 352, 75 N. W. 244 10
Blodgett v. Holden, 275 U. S. 142 158
Board of Commissioners v. Tome, 153 Fed. 81 10
Bourne v. Baer, 107 Nebr. 255 48
Bowers, etc. v. New York & Albany Lighterage Co., 273 U. S. 346, 47 S. Ct. Rep. 389, 71 L. Ed. 676 ..... 37, 60
Brewster v. Gage, ... U. S. 35, 103
Bromley v. McCaughn, 280 U. S. 124 158

Case v. Beauregard, 101 U. S. 688 49
Case v. R. R. Co., 101 U. S. 688 49
Coleman v. Hagey, 252 Mo. 102 9
Cunningham v. City of Cleveland, 98 Fed. 657 43
Curran v. Arkansas, 15 How. 304 50

Dayton Airplane Co. v. U. S., 21 Fed. (2d) 673 114
Dewey v. Coal Co., 123 U. S. 329 44
Dole v. Wilson, 39 Minn. 330, 40 N. W. 161 ..... 10, 44

Eidman v. Martinez, 184 U. S. 578 157
Ex Parte Williams, 297 U. S. 267 69

The Falcon, 19 Fed. (2d) 1009 115
Farmers Bank v. Daiker, 166 Iowa 728 140
Felland v. Wilkinson, 33 Fed. (2d) 961 32
Fisher v. Woodard, 103 Neb. 253 10
Flagg v. Flagg, 39 Nebr. 229 ..... 10, 45
Fogg v. Blair, 133 U. S. 534 9

General Electric Co. v. Hurd, 171 Fed. 984 10
Gould v. Gould, 245 U. S. 151 ..... 16, 151
Graham v. LaCrosse, etc. R. Co., 102 U. S. 148, 26 L. Ed. 106 ..... 9, 12, 14, 131

Hollins v. Brierfield Coal & I. Co., 150 U. S. 371 ..... 9, 12, 14, 132
Holmes v. Webster, 98 Nebr. 105 ..... 10, 45

TABLE OF CASES CITED (Continued)

	Page
Horbach v. Hill, 112 U. S. 144	141
Hospes v. Northwestern Mfg. Co., 48 Minn. 174	9, 14
Houghton v. Axelsson, 64 Kans. 274	44
Johnson v. U. S., 268 U. S. 220	40
Lawrence v. Greenup, 97 Fed. 906, 38 C. C. A. 546	138
Lawrence v. Ham, 19 Fed. (2d) 643	117
Leudecke v. Des Moines Cabinet Co., 140 Ia. 223	9, 134
McAleer v. Clay County, 42 Fed. 665	10
McDonald v. Thompson, 184 U. S. 71	48
McDonald v. Williams, 174 U. S. 397	9, 134
McWilliams v. Excelsior Coal & I. Co., 298 Fed. 884	43
Mattingly v. Nye, 8 Wall. 270	14, 138
Merchants Nat. Bk. v. McDonald, 63 Nebr. 363	10, 42
Mid-Continent v. Alexander, 35 Fed. (2d) 43	33
Mullen v. Hewitt, 103 Mo. 639	10
Mumma v. Potomac Co., 8 Peters 281	50
Newell v. Dart, 28 Minn. 243	10
New Orleans v. Fisher, 100 U. S. 185	44
Old Grove Church v. Rice, 162 Ky. 525	140
Owensboro v. Lucas, 18 Fed. (2d) 798	32
Parker v. Hand, 299 Ill. 420	140
Pennsylvania Steel Co. v. Ry. Co., 198 Fed. 774	16
Pierce v. U. S., 257 Fed. 514	44
Pierce v. U. S., 255 U. S. 398	9, 10, 12, 43
Porter v. Wingert, 200 Ia. 1371	43
Radcliffe v. Clendenim, 232 Fed. 61	141
Railroad Company v. Howard, 7 Wall. 392	50
Ralston v. Heiner, 24 Fed. (2d) 416	32
Robertson v. Perkins, 129 U. S. 333	13
Routzahn v. Tyroler 36 Fed. (2d) 208	33
Russell v. U. S., 278 U. S. 181	37
Sanger v. Upton, 91 U. S. 56	51
Schwab v. Doyle, 258 U. S. 529	16, 153
Scott v. Neely, 140 U. S. 106	10, 46

Page

Scott v. Western Pac. R. Co., 246 Fed. 545 16
Sexton v. Wheaton, 8 Wheaton 229 ..... 14, 137
Shaw v. Robinson & Stokes, 50 Neb. 403 ..... 9, 14, 41, 139
Smietanka v. First Tr. & Sav. Bk., 257 U. S. 602 ..... 16, 146, 150
St. P. M. & M. R. Co., 247 U. S. 310 69
State Bank v. Morse, 60 Kas. 526 13
Stieff v. Tait, 26 Fed. (2d) 489 13
Swan v. Frank, 148 U. S. 603 51
Sweet v. Lang, 14 Fed. (2d) 762 141
Terry v. Anderson, 95 U. S. 628 49
Thomas v. U. S., 22 Fed. (2d) 1000 125
Trinacia v. Clarke, 34 Fed. (2d) 325 ..... 33, 34
U. S. v. Armstrong, 26 Fed. (2d) 227 29
U. S. v. Barth, 279 U. S. 370 38
U. S. v. Carver, 260 U. S. 482 15
U. S. v. Jackson, ... U. S. 35
U. S. v. Lazenby, 5 Fed. (2d) 827 22
U. S. v. Mabel Elevator Co., 17 Fed. (2d) 109 ..... 116, 124
U. S. v. Merriam, 263 U. S. 179 155
U. S. v. Oregon Lmbr. Co., 260 U. S. 290 47
U. S. v. Phellis, 257 U. S. 156 125
U. S. v. Snook, 24 Fed. (2d) 844 29
U. S. v. Whited & Wheless, 246 U. S. 552 46
U. S. v. Whitridge, 231 U. S. 144 156
Untermyer v. Anderson, 276 U. S. 440 158
Updike, et al., v. U. S., 8 Fed. (2d) 913 15
Whitman v. Oxford Bank, 176 U. S. 559 49
Wood v. Bank, 24 Fed. (2d) 661 141
Wood v. Carpenter, 101 U. S. 135 59

BOARD OF TAX APPEALS DECISIONS

	Page
**Bastrop v. Commissioner*, 7 B. T. A. 529	116
Belowsky v. Commissioner, 7 B. T. A. 424	117-118
**Cohn & Sons Co. v. Commissioner*, 9 B. T. A. 87	68
Colmer-Green Lbr. Co., 12 B. T. A. 256	121
**Conrad Hdw. Co. v. Commissioner*, 8 B. T. A. 512	123-124
**Fibre Container Co. v. Commissioner*, 9 B. T. A. 575	120
**Franklin v. Commissioner*, 7 B. T. A. 636	116
**Hammersly v. Commissioner*, 16 B. T. A. 68	28
Hynes v. Commissioner, 16 B. T. A. 1272	28
**Appeal of F. A. Hall Co.*, 3 B. T. A. 1172	120
Indiana Rolling Mills Co. v. Commissioner, 13 B. T. A. 1147	120
**Kellogg Commission Co. v. Commissioner*, 6 B. T. A. 771	120
Lancaster Lens Co. v. Commissioner, 10 B. T. A. 1153	117
Lowenstein Bros. Garment Co., 13 B. T. A. 446	122
Appeal of National Refining Co., 1. B. T. A. 236	117
Appeal of National Tank & Export Co., 3 B. T. A. 1217	121
Paso Robles Merc. Co., 12 B. T. A. 750	122
Shanley v. Commissioner, 7 B. T. A. 521	117
**Spencer v. Commissioner*, 11 B. T. A. 437	28
Stetson & Ellison v. Commissioner, 11 B. T. A. 397	122
**Appeal of Washburn*, 7 B. T. A. 483	123
**Werbelovsky, Ex. v. Commissioner*, 8 B. T. A. 442	100-101
**Wheeler v. Commissioner*, 16 B. T. A. 96	28
Willingham L. & T. Co., 15 B. T. A. 931	122

* Indicates decisions acquiesced in by Commissioner.

GENERAL COUNSEL'S MEMORANDA

Page

G. C. M. 1029 VI-2, 95 24-25

2939 VII-6-3597 67

4554 VII-2, 86 26-27

REVENUE LAWS

Revenue Act of 1916:

Sec. 13 (b) (39 Stat. 771) 104-161
14 (a) (39 Stat. 772) 125
14 (b) (39 Stat. 772) 126
19 (39 Stat. 776) 105

Revenue Act of Oct. 3, 1917:

Sec. 4 (40 Stat. 302) 74-105-106
200 (40 Stat. 302) 106-142-162
212 (40 Stat. 307) 74-162
1004 (40 Stat. 325) 107
1005 (40 Stat. 326) 107
1302 (40 Stat. 338) 142-162

Revenue Act of 1921:

Sec. 250 (d) (42 Stat. 265) 54-71-99

Revenue Act of 1924:

Sec. 277 (a) (2) (43 Stat. 299) 71-72
278 (a) (43 Stat. 299) 54-99
278 (d) (43 Stat. 300) 52
1009 (b) (43 Stat. 341) 53
1009 (c) (43 Stat. 341) 53

Revenue Act of 1926:

Sec. 278 (a) (44 Stat. 59) 54-99
278 (d) (44 Stat. 59) 18
280 (a) (44 Stat. 61) 20
1109 (a) (1) (2) (3) (44 Stat. 114) 127-128

Sec. 2, Ch. 1, Title 26, U. S. Code 108

Sec. 3173, R. S. U. S., as amended by Sec. 16, Rev. Act 1916.... 104

REGULATIONS BUREAU OF INTERNAL REVENUE

Page

Reg. 33, Art. 196 79-80-164
33 (Rev.), Art. 61 109-162-163

MISCELLANEOUS CITATIONS

Conference Report to the House, pp. 43, 44, on Rev. Bill of 1926..... 21-22

Conference Report to House, on Rev. Act of 1926, p. 42, dated Feb. 22, 1926 69

Report of Joint Committee on Internal Revenue Taxation on Sec. 280, Vol. I, p. 67 25-26

Report of Committee on Finance of Senate upon Rev. Act of 1924, pp. 35, 40, 41, 49, 50, 51, 52..... 62-63-64-65-66

Report of Committee on Ways and Means of the House, p. 12, on Rev. Act of 1926, dated Dec. 7, 1925..... 69

Senate Finance Committee Report, dated May 1, 1928, p. 32, on Sec. 278 (d) Rev. Act 1928 29

Ways and Means Committee Report to the House, dated Dec. 7, 1927, p. 24, on Sec. 278 (d) of Rev. Act of 1928..... 29

Sec. 447, Comp. St. Neb. 1922..... 164

Sec. 453, Comp. St. Neb. 1922..... 163

Sec. 468, Comp. St. Neb. 1922..... 144-163

Sec. 700, Comp. St. Neb. 1922..... 144-163

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR NELSON B. UPDIKE, ET AL., RESPONDENTS

NATURE OF THE SUIT

This is a proceeding to collect a tax upon the income of Updike Grain Company, dissolved in August, 1917, from the transferees of the assets of that company, for the period January 1, 1917, to June 30, 1917, which was

assessed against the Updike Grain Company in January, 1920, upon returns filed by the Updike Grain Company in August, 1917.

QUESTIONS PRESENTED

1.

The collection of the sum sought to be recovered herein from the defendants, as transferees of the assets of the Updike Grain Company, is barred by Section 278 (d) of the Revenue Act of 1926.

2.

The collection of the sum sought to be recovered herein from the defendants, as transferees of the assets of the Updike Grain Company, is barred by Section 250 (d) of the Revenue Act of 1921 and Section 277 of the Revenue Act of 1924.

3.

If the collection of these taxes by proceedings of any kind against the taxpayer is barred by the limitations contained in any of the revenue acts, the suit cannot be maintained against the transferees as an independent suit for the recovery of trust funds.

4.

The suit against the transferees cannot be maintained in any case, because the Government is a subsequent creditor as to the transfer in August, 1917,

there being at that time no tax liability nor an existing statute under which a tax liability could arise.

5.

The provisions of the Revenue Act of October 3, 1917, are not applicable to a corporation which was lawfully dissolved under state law, after having discharged all its existing obligations and distributed all its assets among its stockholders prior to the enactment of the suit.

STATEMENT OF FACTS

While the statement contained in the Government's brief is only inaccurate, in that it is stated on page 4 that no returns were ever filed in behalf of the corporation under the Revenue Act of 1917, and on page 5 that the present suit was begun under the "trust fund" doctrine to recover "funds" received by the stockholders to the use of the United States, yet it omits portions of the record necessary to a full understanding of the issues presented by the respondents here. It is necessary, also, to restate some of the statutes attached in the appendix to the Government's brief, because they omit portions relied upon by the respondents on this appeal; and it is also necessary to add some additional sections.

The Updike Grain Company was a corporation organized under the laws of the State of Nebraska, and it was dissolved pursuant to those laws during the month of August, 1917. Prior to its dissolution it had paid all

its debts and obligations of every character, including all taxes which had accrued, or could accrue, to the Government of the United States under the existing revenue laws (R. 91, 127). As stated, it distributed in cash its capital stock amounting to $2,000,000.

Under the revenue laws of 1913 and 1916, the Updike Grain Company had selected a fiscal year as the basis of its federal taxation, and, pursuant to proper procedure, its fiscal year terminated on June 30, 1917 (R. 161). Within sixty days thereafter it filed returns, an income tax return on Form 1031 (Revised October 1916) and profits tax return on Form 1095, pursuant to the provisions of Sec. 13 (b) of the Revenue Act of 1916, fully set forth in the appendix to this brief. The income shown in those returns is the sole basis of the claim of the Government for the taxes accruing under the Act of October 3, 1917. Although the corporation remained in existence after June 30, 1917, until its dissolution in August of that year, yet it is not claimed by the Government that it transacted any business, nor is any claim made for taxes accruing after that period. Not only did the taxpayer report fully and honestly to the Government, all income received by it, and every fact, regarding the income, called for by existing regulations, (R. 107) but, by an unintentional error in calculation, it reported a greater income than it was actually taxable for, and the effect of the Government's audit was to reduce the taxable income of the taxpayer for that period (R. 113, 145).

It is true that Form 1031 (revised January, 1918) was mailed to the taxpayer, and received by its former secretary, in March, 1918. But he immediately returned it with a letter stating that the corporation was dissolved and that it had filed its return showing all the income which it had received up to the time of its dissolution, and had paid all taxes accruing to the United States Government under existing laws and regulations, and also called attention to the fact that subsequent to its dissolution it had made final and fiscal returns, showing all its income (R. 91). Thereafter no action was taken by the Bureau of Internal Revenue under Regulation 33, Article 196, in effect from January 6, 1914, to December 31, 1921, which is included in the appendix to this brief, by sending to the taxpayer a notice on Form 1045, or by making other demand for returns (R. 349).

During the month of October, 1918, an agent of the Internal Revenue Bureau examined the books and records of the Updike Grain Company for the years 1913, 1914, 1915, 1916, and 1917, to determine its tax liability for said years, and the fiscal period in 1917 ending June 30, 1917 (R. 95). When he called at the former office of the company and conferred with its former secretary he asked for copies of the returns which the company had made for the fiscal year ending June 30, 1917, and these were furnished him. (R. 350). The agent made up returns upon the forms then in effect, a corporation income tax return on Form 1031, revised January, 1918, and a corporation excess profits tax return on Form 1103 (R. 131-35). These returns were not signed, but it is significant that the agent of the Bureau, in preparing and

transmitting them, (to the commissioner), denominated them "amended returns." In his report to the Department (R. 107) the agent sends in the draft of amended returns, unsigned. When this report was transmitted by the Omaha office to the Commissioner's office in Washington, it was accompanied by a letter (R. 105) in which the agent's action is referred to as a report "of the returns of annual net income of the Updike Grain Company." In subsequent correspondence between the Omaha office and the Washington office on the subject (R. 101) this report of the Revenue Agent is referred to as "supplemental return, fiscal year ended June 30, 1917." In a letter from the Revenue Agent in Charge at Omaha to the Updike Grain Company (R. 317) and another letter of November 24th, 1919 (R. 323), and in various copies, reports, official actions and records, this return, made by the Updike Grain Company, within sixty days from the close of its fiscal year ending June 30, 1917, is referred to as the return of the corporation for the taxable period then under consideration, and all the transactions of the Government officials concerning it are treated and discussed as amendments or investigations or revisions of that return, and, finally, in January, 1920, the Commissioner of Internal Revenue assessed a tax against the Updike Grain Company for the amount now sought to be collected in this suit, and, among other entries in the Government records, stamped upon the original returns of the company made within sixty days of the end of its fiscal year, a stamp indicating the assessment, and containing in figures the amount (R. 165).

The defenses presented in the lower court were that no tax ever accrued against the Updike Grain Company, that the stockholders were not liable for the subsequent obligations of the company, if any existed, and that the suit was barred by the provisions of the revenue laws of 1921, 1924 and 1926.

SYNOPSIS OF ARGUMENT

I.

The appellees contend that this suit is barred by the provisions of Section 278 (d) of the Revenue Act of 1926 for the reason that this is a proceeding to collect a tax; the tax was assessed against the taxpayer in January, 1920; and this suit was commenced on April 2, 1927, more than seven years after the assessment. Even if no return had been filed by the taxpayer, nevertheless, a collection of the assessment is barred after the lapse of six years, because the clause in the section making it applicable to an assessment made "within the statutory period of limitation properly applicable thereto", when construed in connection with the other legislation on the subject, was obviously inserted for the protection of the taxpayer, to prevent this section from operating to authorize a suit against the taxpayer upon an assessment made after the time for making it had been barred by the provisions of any section of the revenue law. Moreover, the phrase "within the statutory period" is obviously, and in the light of the context, applicable to that indefinite period during which the Commissioner is authorized to assess a tax against a tax-

payer who has failed to file a return. Congress has included the clause "at any time", by reference, as one of the cases within which an assessment may be made, and afterwards barred. The proceedings in Congress, as appears from the report of the Conference Committee, and other proceedings there, indicate that Congress intended by this section to bar suits upon assessments, even though there had been no limitation upon the time for making an assessment. This assessment was made within a period of limitation applicable thereto, as stated in the opinion of the District Court, because at the time it was made there was a limitation of three years, that is, from March 15, 1918, to March 15, 1921, within which it was necessary for the Commissioner to discover the deficiency and thereafter make the assessment. The discovery in this case was made within three years and the assessment which followed was, therefore, within a statutory period applicable to it. This was the construction placed upon this section by the Internal Revenue Bureau during its enactment, and afterwards, until a short time before the commencement of this suit. In numerous hearings before the Board of Tax Appeals, and in decisions of the district and circuit courts, including the decision appealed from here, this has been the uniform construction placed upon this section.

The attempted application by the Government of the "trust fund theory" to this case, will not authorize the prosecution of the suit, if it is determined by the court that a suit against the taxpayer would have been barred by the provisions of Sec. 278 (d) of the Revenue Act of 1926, or by any earlier provisions of the revenue

laws; for the reason that the trust fund theory, in the form propounded by the Government in its argument, has been expressly repudiated by this court in *Graham vs. Railroad Co.*, 102 U. S. 148; *Fogg v. Blair*, 133 U. S. 534; *Hollins v. Brierfield Coal & Iron Co.*, 150 U. S. 371; *McDonald v. Williams*, 174 U. S. 397; *Pierce v. United States*, 255 U. S. 398, and by state decisions in *Shaw v. Robinson & Stokes*, 50 Neb. 403; *Coleman v. Hagey*, 252 Mo. 102; *Leudecke v. Des Moines Co.*, 140 Ia. 223, and *Hospes v. N. W. Mfg. Co.*, 48 Minn. 174, as well as in numerous other decisions. It does not apply to this case in any event, because the primary question here is not the application of a statute of limitations to the suit against the transferees, but to the absence, in the plaintiff's case, of a fundamental prerequisite for the prosecution of a suit against the transferee, to-wit, the existence of a present enforceable claim against the transferor. But, in any case, a suit against the transferee is a proceeding in court for the collection of a tax within the meaning of Sec. 278 (d), as appears from the Government's petition in this case (R. 8), even after it had been amended for the purpose of converting it into a general equity suit (R. 12-155, 6, 7-160), because it is based upon the averment that the tax accrued against the taxpayer, and that the property in the hands of the transferees is liable to the payment of that tax, and the prayer is that the amount of the tax be recovered. As such a suit is, in its essence, a creditor's bill, it is ancillary to the claim upon which it is based, and a part of the proceedings for the collection of the tax. A creditor's bill has been called an equitable execution, and whether it is invoked in aid of the collection of a judgment at law,

where execution fails, or in aid of the collection of a tax against the transferor, if such a suit is permissible without a judgment at law, it remains essentially an ancillary proceeding, which, in no case, can rise higher than its source, or be enforceable after the claim upon which it is founded ceases to be enforceable against the transferor. *Merchants Nat. Bk. vs. McDonald,* 63 Neb. 363; *Pierce vs. United States,* 255 U. S. 398; *Dole vs. Wilson,* 39 Minn. 330; *Flagg vs. Flagg,* 39 Neb. 229; *Holmes v. Webster,* 98 Neb. 105; *Fisher v. Woodard,* 103 Neb. 253; *Newell v. Dart,* 28 Minn. 243; *Scott v. Neely,* 140 U. S. 106; *Bank v. Braithwaite,* 7 N. Dak. 352; *McAleer v. Clay Co.,* 42 Fed. 665; *Board v. Tome,* 153 Fed. 81; *Gen. Elec. v. Hurd,* 171 Fed. 984; *Mullen v. Hewitt,* 103 Mo. 639.

But the appellees contend that this is not a no return case, and urge that the right to collect this tax became barred by the provisions of Section 277 of the Revenue Act of 1926. Under the statutes as they existed in 1917 and 1918, the only law requiring a return from a corporate taxpayer having a fiscal year, was found in Section 13 (b) of the Revenue Act of 1916, which provided that such corporations should file their returns within sixty days after the close of their fiscal year, and, by the provisions of Section 4 of the Revenue Act of 1917, which provided that the increased income tax authorized by that act should be computed, assessed and collected upon the same incomes, and in the same manner as the taxes imposed by the Act of 1916, and by Section 212 of the Excess Profits Tax of 1917, it was provided that all provisions of the 1916 law relative to returns,

were made applicable to the tax imposed by the new act. Under these statutes the appellees contend that the filing of their returns within sixty days of June 30, 1917, was a compliance, not only with the 1916 Act then existing, but also fulfilled the provisions of the Act of October 3, 1917, which merely adopted the 1916 law relating to returns, and neither the revenue acts, nor any distinct and unambiguous provision found in the Treasury Regulations, required a corporation which had reported its income within the statutory period, to file new and independent returns after the passage of the Act of October 3, 1917.

But whether the returns so filed constituted such compliance with the law, in and of themselves, as to constitute the basis for the running of the statute of limitations found in the 1921 Act, and in the 1926 Act, yet the conduct of the Government officials with reference to returns, by which they were accepted and treated as the returns required by the Act of October 3, 1917, and were audited as such, and the assessment of January, 1920, was made upon those returns, after the Government had audited them and found them correct, and by treating these returns as the statutory returns upon which the limitation was based, until the first of those series of cases was pending in court. The point here is that the Government, having from the very beginning treated this return as the statutory return, and at no time required the taxpayer to file any other return or requested any other than an amendment to this return, the Government ought not now be permitted to change

front for the purpose of evading the subsequent statute of limitations.

No claim is made against the respondents solely because they are stockholders of the corporate taxpayer, it is not claimed that there is any statute of the State of Nebraska, where the corporation is organized, that makes them liable, and there is no statute of the United States which makes them liable as stockholders, or as transferees of the corporate assets; not even Sec. 280 attempts either to create or enlarge the liability of transferees of assets, but merely regulates a procedure for enforcing by summary process whatever existing liability there may be at law or equity. Necessarily, therefore, whatever liability exists is that which grows out of the laws of Nebraska, including such general rules of law as are construed and defined in the courts of the United States with reference to transactions arising under the laws of the State of Nebraska. The liability to creditors growing out of the transfer of assets of a corporation to its stockholders is, in a proceeding of this character, precisely the same as the liability of the transferee of assets of an individual. (*Graham v. Railroad Co.*, 102 U. S. 148; *Hollins v. Brierfield*, 150 U. S. 371; *Pierce v. United States*, 255 U. S. 398). It is only when a court of equity has taken over the liquidation of a corporation, that there is any trust which differs from the status of the transferred assets of an individual debtor and the claims of the creditors. In each case the right of the creditor to pursue the assets is a remedy granted to the creditor because of the inadequacy of legal remedies, either because a judgment at law and the failure of execution

has demonstrated the insufficiency of the legal remedies, or because a court of equity, in administering the remedy directly, without a prior judgment at law, has become satisfied that there is no remedy in the proceedings at law, and that the remedies in equity are therefore available. But it is universally held in the decisions defining and enforcing this equitable remedy, that it is available only to a creditor existing at the time of the transfer. This is true whether the transfer was fraudulent as against existing creditors, or whether it was only voluntary, and therefore capable of being set aside by existing creditors. But in no case is the remedy available to a subsequent creditor, unless, in some jurisdictions he can allege and prove that the transfer was made in contemplation of a debt to be contracted and was intended as a fraud upon such creditor. In this case there is no allegation of any intention on the part of the corporation or its stockholders to defraud the Government by distributing its assets and dissolving in August, 1917, but, on the contrary, the averment is that the dissolution was "duly" made (R. 9), that the resolution of the stockholders providing for dissolution of the corporation and the transfer of its assets was "duly" adopted by the stockholders, and that thereafter (R. 10) legal steps to complete the dissolution were "duly" taken. Of course, the meaning of the word "duly" is that the steps were lawfully taken, (Century Dictionary, Standard Dictionary, 19 C. J. 833, *State Bank v. Morse*, 60 Kas. 526; *Robertson, Col. v. Perkins*, 129 U. S. 333) and it is no where alleged that they were taken unlawfully and for the purpose of defrauding the Government, nor is there any proof whatever to that effect. The averment in the Government's

petition that the action of the corporation was "duly" taken, applies as well to the resolution directing the distribution of the assets among the stockholders, as to the technical steps relating to the dissolution itself.

The right to pursue the assets of a debtor to satisfy the claims of a creditor, as distinguished from the procedure, is based upon Statute 13, Eliz. c5, and the various statutes of the states re-enacting that statute, with modifications or enlargements. (*Sexton v. Wheaton,* 8 Wheat. 229, *Mattingly v. Nye,* 8 Wall. 370; *Graham v. Railroad Co.,* 102 U. S. 148; *Hollins v. Brierfield,* 150 U. S. 371; *Shaw v. Robinson & Stokes,* 50 Neb. 403; *Hospes v. N. W. Mfg. Co.,* 48 Minn. 174). And under these decisions, the right of the creditor is grounded upon the statute, and applies alike to the creditors of an individual and the creditors of a corporation.

If the action against the taxpayer was barred by Sec. 278 (d) of the Revnue Act of 1926, then the Government cannot succeed in this proceeding, because it lacks an essential element in its case, that is, a debt existing at the time of the suit, and whether barred by that section or not, the Government cannot recover against the stockholders, because it is a subsequent creditor, and not in a position to attack a transfer completed before the Government's claim was even authorized by a statute.

While it is true that the decisions of various district courts and circuit courts of appeal are to the effect that a corporation lawfully, that is "duly," dissolved in 1917, prior to the passage of the act of October 3, 1917, is liable to the increased tax imposed by that act, yet this court has no where so decided, and its refusal

to grant a certiorari in the first case of *Updike v. United States,* 8 Fed. (2nd) 913, 271 U. S. 661, does not imply any approval by this court of the decisions of the district or circuit court in that case, and certainly not in any of the other cases which did not reach this court. (*United States vs. Carver,* 260 U. S. 482).

In accordance with the first ruling made by the Commissioner of Internal Revenue in October, 1917, after the passage of the act (R. 187), the stockholders of the Updike Grain Company have contended that the act of October 3, 1917, was not applicable to a corporation which was dissolved before the act was passed, because, whether it was in the power of Congress or not, no intention was shown in that act to revive a dissolved corporation for the purpose of taxing it. By the final section of the act, 40 Statutes at Large, 338, §1302 it was provided that, unless as otherwise provided in the act, it should take effect and be in force on the day after its passage, and as it was passed on October 3 ,1917, it took effect and became in force on October 4, 1917. So far as affects this controversy, the only feature of the act which could be called retroactive, are the provisions of Sections 4 and 200 of the act, (40 St. at L. 302) to the effect that the first taxable year under the act should be the year 1917, and that for corporations having a fiscal year, the first taxable year should be the fiscal year ending during 1917. That Congress thereby declared an intention of applying the terms of the act to all incomes during any part of the calendar year 1917, is conceded, but the contention of the stockholders at all times has been that the statute no where evinced an intention of taxing cor-

porations which have passed out of existence, nor the transferees or stockholders of such corporations, conceding to the fullest extent the power of Congress to do so, if it had indicated its intention to take such action. The income tax is a personal tax; it is in no sense a levy upon specific property. All the provisions of the law indicate that it creates a personal liability on the part of persons and corporations, and its failure to specify that its terms are applicable to the stockholders of dissolved corporations, under the familiar rule that a tax statute will not be extended by implication, means that a tax was not assessable on account of income received by a defunct corporation. *Smietanka v. Trust & Savings Bank,* 257 U. S. 602; *Schwab v. Doyle,* 258 U. S. 529; *Union Trust Co. v. Wardell,* 258 U. S. 537; *Gould v. Gould,* 245 U. S. 151, *Anderson v. Railway Co.,* 216 Fed. 83 (C. C. A. 2d Circuit), (Excise Tax of 1909); *Scott v. Railway Co.,* 246 Fed. 545 (C. C. A. 9th Circuit); *Pa. Steel Co. v. Railway Co.,* 198 Fed. 774 (C. C. A. 2d Circuit).

ARGUMENT

I.

Was the collection of the sum sought to be recovered herein from the defendants, as transferees of the assets of Updike Grain Company, barred by section 278 (d) of the Revenue Act of 1926 at the time this action was begun?

The Government's brief contains two reasons for contending that Section 278 (d) does not bar this suit, which may be summarized as follows:

1. Because this is not a proceeding to collect taxes.
2. Because the taxpayer filed no return, in which case the tax could have been assessed "at any time", which is not a "statutory period of limitation properly applicable thereto."

We will discuss these two contentions under numerals 1 and 2.

1.

This contention is sought to be supported with three reasons which we shall discuss under letters (a), (b) and (c), with headings as summarized in the Government's brief, pp. 7 and 8.

(a).

> "That Congress intended Section 278 (d) of the Revenue Act of 1926 to be so restricted is indicated by the fact that in Section 280, authorizing the Commissioner to notify transferees of corporate assets of deficiencies in a tax against the corporation, and giving them the right of appeal to the Board of Tax Appeals, specific statutes of limitation were enacted." (p. 7, Gov. brief).

The applicable part of Section 278 (d) to this argument is as follows:

> "Where the assessment of income, excess profits, or war profits tax imposed * * * by prior act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax."

The following concessions are made by the petitioner in its brief or are undisputed in the record:

1. That the amount sought to be recovered herein represents income, excess profits and war profits taxes imposed by a prior Act of Congress, to-wit: The Revenue Act of 1917. (Gov. Brief, 4).

2. That the taxes were assessed against the taxpayer before the enactment of the Revenue Act of 1926. (Gov. Brief, 4).

3. That the taxes were assessed in January, 1920. (Gov. Brief, 4).

4. That this suit was begun April 2, 1927, more than six years after the assessment of the taxes was made. (Gov. Brief, 5).

5. That no other suit or proceedings has been begun against the taxpayer, the stockholders or any one else, for collection of the taxes. (Gov. Brief, 5).

6. There were no waivers or consents by the taxpayer or any one else, extending the time for assessment or collection of the taxes.

If this is a proceeding to collect taxes this case comes squarely within the terms of the above section.

It is also apparent that the right to proceed against the taxpayer for the taxes involved became barred by this section in January, 1926. and if the Government had proceeded against the respondents under Sec. 280, that right became barred in January, 1927, more than two months before this proceeding was begun; also that the right to proceed against the taxpayer having become barred before the enactment of the Revenue Act of 1926, the liability for the tax was extinguished by Sec. 1106 Revenue Act of 1926.

The Government seeks to avoid the application of Section 278 (d) under this subdivision of its argument by the contention that although its terms are broad enough to bar this suit, and do not limit its application to proceedings against the taxpayer only, Congress by enacting "specific statutes of limitation" in Section 280, of the same Revenue Act, indicated an intention to restrict the application of Section 278 (d) to proceedings against the taxpayer only.

Bearing in mind that this is a proceeding to "collect" and not to "assess", and that Section 278 (d) deals solely with the right to "collect", it is, therefore, necessary for us to ascertain (1) if Congress did in fact restrict the effect of Section 278 (d) by any "specific stat-

utes of limitation" in Section 280, and (2) the intention of Congress.

Section 280 deals with limitations upon both the right to "*collect*" a tax from, and the right to "*assess*" a tax against, a transferee, but it deals with the right to "*collect*", only in the general terms of Paragraph (a) thereof, wherein the general limitation statutes of the Revenue Acts were made applicable, to proceedings thereunder against transferees, by the use of the following language:

> "The amounts * * * shall except as hereinafter in this Section provided, be assessed, *collected,* and paid in the same manner and subject to the same provisions and *limitations* as in the case of a deficiency in a tax imposed by this title (* * * including * * the provisions authorizing distraint and proceedings in court *for collection*). (Our italics).

Note the phrase "except as hereinafter in this Section provided." Thereinafter there was no provision otherwise limiting the time "*for collection*", but there were specific provisions changing the time for "*assessments,*" which simply extended "the period of limitation for *assessment* of any such liability" to "within one year after the expiration of the period for *assessment* against the taxpayer", or if an assessment had been made against the taxpayer before the time for assessing him had expired, to any time within six years after the assessment, but in no case later than one year after the enactment of the 1926 Act, to-wit: February 26, 1926. (Sec. 280 (b) (1) (2), Rev. Act of 1926).

It must be quite clear from an analysis of Section 280 that Congress expressly made proceedings thereunder both to collect and assess subject to limitation statutes contained in other sections of the Act and particularly in Section 278 (d). If this conclusion admits of any doubt, the intention of Congress in that respect is made plain at pp. 43 and 44 of the Conference Report to the House of Representatives on the Revenue Bill of 1926, dated February 22, 1926, wherein, in discussing the purport of Section 280, it is stated:

> "Without in any way changing the extent of such liability of the transferee under existing law, the amendment enforces such liability (whether in respect of the tax as originally returned by the taxpayer or a deficiency therein) in the same manner as liability for a tax deficiency is enforced; that is, notice by the Commissioner to the transferee and opportunity either to pay and sue for refund or else to proceed before the Board of Tax Appeals, with review by the courts. Such a proceeding is in lieu of the present equity proceeding and is exclusive, save that, of course, in a proper case, a tax lien upon the assets arising prior to their transfer may be enforced against the transferee by distraint, or in case of real estate by a proceeding in equity. In the case where the taxpayer remains in existence after the transfer, an unsatisfied return of a distraint warrant, issued in pursuance of an assessment lawfully made after a deficiency letter has been mailed to the taxpayer, would suffice in lieu of an unsatisfied execution to establish the liability of the taxpayer.
>
> "In view of the above situation it will be seen that the amendment makes the procedure for the collection of the amount of the liability of transferees conform to the procedure for the collection of taxes. The amendment thereby substitutes the specialized and more expeditious procedure of the board for

that of the district courts in equity and will develop through the board a uniformity of precedents in lieu of the present rather vague principles of law governing the liability of a transferee for unpaid taxes of a transferor.

* * * * *

"Under the amendment the liability of the taxpayer for the tax, including all interest and penalties, is fixed as of the time of the transfer of the assets.

* * * * *

"*The statute of limitations as to collection is covered by the incorporation by reference of section* 278 (d). (Our italics)

The last sentence is significant inasmuch as Section 278 (d) was not specifically mentioned in Section 280.

The Bill as reported by the Conference Committee was enacted into law February 26, 1926. Thereafter the procedure outlined in Section 280 was almost universally adopted by the Commissioner in all proceedings for collection of taxes from transferees.

Prior to the passage of the 1926 Act it was the uniform holding of the courts that when a claim under the trust fund theory became barred against the transferor, it thereupon and thereby became unenforcible against the transferee (see cases infra) and this general rule had been applied to claims for income taxes.

In *United States vs. Lazenby,* 5 Fed. (2d) 827, (D. C. N. D. Texas), decided June 3, 1925, being an action by the Government against transferees of the assets of a dissolved corporation to recover income taxes of a dissolved corporation for the year 1918, the court said:

"That the instant suit is not against the original taxpayer, but is at equity against a person who received all of the assets of the taxpayer, must not prevent a reasonable view of the statute of repose which Congress evidently intended. The language of the statute is that 'no proceeding in court for the collection of such taxes shall be begun after the expiration of such period.' Certainly there can be no other object in the present suit. It is for the collection of a tax. While I do not think that a narrow construction of the statute should be made, I am of the opinion that the first two criticisms of the motion to dismiss are well taken."

Congress indicated its understanding of this rule and expressly provided in Section 280 (a) that it should apply to proceedings to collect taxes from transferees, and modified it only with respect to proceedings to assess the liability for taxes against a transferee. In the fall of 1926 this point was raised by the respondents herein in a hearing, as to their liability for the taxes herein involved, had before representatives of the office of the General Counsel of the Bureau of Internal Revenue, and on Dcember 7, 1926, D. H. Blair, Commissioner of Internal Revenue wrote to the attorney for Mr. Updike, as follows:

"Receipt is acknowledged of your letter addressed to the General Counsel under date of November 20, 1926, concerning the matter of the income tax liability of the Updike Grain Company.

"It has been decided that no steps will be taken to assess against Mr. Updike any liability of the Updike Grain Company as provided in Section 280 of the Revenue Act of 1926." (R. 44).

On December 31, 1926, C. R. Nash, Assistant to the Commissioner, in a letter to the Collector of Internal Revenue, Omaha, Nebraska, after referring to the tax sought to be collected herein, said:

> "This office has decided that there is no liability which can be asserted against Mr. Nelson B. Updike, Omaha, Nebraska, et al, as transferees of the property of the taxpayer, pursuant to the provisions of Section 280 of the Revenue Act of 1926. The amount of tax set forth above should, therefore, be abated as uncollectible on Form 53." (R. 291).

Thereafter A. W. Gregg, General Counsel of the Bureau of Internal Revenue, in G. C. M. 1029, Cum. Bull. VI-2, 95, promulgated on January 10, 1927, an opinion for the guidance of collectors, revenue agents and other employees of the Treasury Department, reaffirming this settled rule, wherein, in construing Section 280, he said:

> "The statute is silent as to whether a transferee may be assessed where the period of limitation for assessment against the taxpayer expired prior to the enactment of the Revenue Act of 1926 without any assessment against such taxpayer having been made or without any proceeding in court against him having been begun.
>
> * * * * *
>
> "Was it intended by Congress that Section 280 should have a retroactive application? That is, was it the purpose of Congress in enacting the Revenue Act of 1926 to make effective, as against a transferee, a tax liability which could not be asserted under the law against the transferor taxpayer because of the bar of the statute of limitation? (See section 278 (e), Revenue Act of 1926.)
>
> "There is nothing in the section itself, or in any portion of the Revenue Act of 1926, or in the legis-

lative history of the Act, which indicates that Congress intended that any liability of the taxpayer which could not be asserted should be made effective by the provisions of section 280 against the transferee of the taxpayer's property.

* * * * *

"Prior to the enactment of the Revenue Act of 1926 there was no statutory authority for assessing transferees of taxpayers' property to satisfy taxes due or found to be due to the United States. True it is that in some instances the amount of taxes was recoverable by suit from transferees where the facts showed they were proper parties to the proceedings by reason of the application of the trust-fund doctrine, but there was no existing statute which gave the right to assess against a transferee amounts due the United States as taxes for which his transferor was primarily and immediately liable. Such right was given for the first time by Section 280 of the Revenue Act of 1926. Under that section the transferees' liability is no greater nor more comprehensive than that of the transferor taxpayer. The section merely prescribes a method for the enforcement of an established liability and adopts, for this purpose, the method of assessment applicable to the collection of taxes in the ordinary case. *The logical conclusion is that it was not the purpose of Congress to make effective against a transferee a tax liability which at the time of the enactment of the Revenue Act of* 1926 *could not be asserted against the transferor taxpayer because of the bar of the Statute of Limitations.* (Our italics)

The Board of Tax Appeals in numerous cases, expressly acquiesced in by the Commissioner of Internal Revenue, made the same ruling.

The Joint Committee on Internal Revenue Taxation, established under Section 1203 of the Revenue Act of

1926, in their report dated November 15, 1927, and with knowledge of these rulings, made no recommendation to change what had become the settled practice of the Treasury Department and the Bureau of Internal Revenue, particularly, because on p. 67, in referring to the effect of Section 280 upon transferees, they said:

> "In substance it subjects him to the same proceedings as though he were the taxpayer",

and on p. 68 said:

> "At present no change is recommended as to limitation proceedings."

The General Counsel of the Bureau of Internal Revenue thereafter continued to adhere to this rule.

In an opinion by Mr. C. M. Charest, General Counsel, promulgated August 13, 1928, in G. C. M. 4554. Cum. Bull. VII-2, 86 he said:

> "An opinion is requested as to whether the amount of the liability of a transferee based on the tax due from the M Company for the period January 1, to February 28, 1918, which was paid by the transferee, the O Company may be credited or refunded to the latter company.
>
> "The liability involved in this case was assessed against the O Company as transferee of the assets of the M Company, under the provisions of Section 280 of the Revenue Act of 1926, but the assessment was made after the expiration of the statutory period applicable thereto. The O Company paid the amount of the assessment and immediately thereafter filed a claim for refund of the amount so paid.
>
> * * *

"It appears unnecessary in the consideration of the question to refer to the decision of the Supreme Court of the United States in the case of *Bowers vs. New York & Albany Lighterage Co.*, since the proposition of crediting or refunding the amount of tax assessed or paid after the expiration of the statutory period is now governed by Section 607 of the Revenue Act of 1928, which provides as follows:

> Any tax (or any interest, penalty, additional amount, or addition to such tax) assessed or paid (whether before or after the enactment of this act) after the expiration of the period of limitation properly applicable thereto shall be considered an overpayment and shall be credited or refunded to the taxpayer if claim therefor is filed within the period of limitation for filing such claim.

"Under the provisions of section 280 of the Revenue Act of 1926 and section 311 of the Revenue Act of 1928, the assessment, collection, and payment of the liability, at law or in equity, of a transferee of the property of a taxpayer are subject to the same provisions and limitations as if a deficiency in tax were involved, except with respect to the period during which an assessment may be made.

"Since the liability involved in the instant case was assessed after the expiration of the statutory period properly applicable thereto, the amount paid in respect to the assessment must be regarded as an overpayment. A claim for refund of such overpayment having been filed within the statutory period, the amount of the overpayment must be credited or refunded."

It will be noted that the General Counsel, accorded to the transferee the rights granted in Section 607, quoted above, although such rights by that section only related to *"any tax"* and were only given to the *"taxpayer."*

The Board of Tax Appeals has continuously adhered to the same rule.

Spencer vs. Commissioner, 11 B. T. A. 437, decided April 9, 1928, acquiesced in by Commissioner, Int. Rev. Bul. VII-31-3828.

Hammersly vs. Commissioner, 16 B. T. A. 68, decided April 18, 1929, acquiesced in by Commissioner, Int. Rev. Bul. VIII-29-4274.

Wheeler vs. Commissioner, 16 B. T. A. 96, decided April 22, 1929, acquiesced in by Commissioner, Int. Rev. Bul. VIII-31-4290.

Hynes vs. Commissioner, 16 B. T. A. 1272, decided June 29, 1929 approving and following opinion of Circuit Court of Appeals in this case.

In the Government's brief, page 19, it is said that Bureau rulings and Board decisions are not in point because they were made with reference to proceedings against transferees under Section 280, but in that the Government is in error because in G. C. M. 1029, supra, and in *Spencer vs. Commissioner,* it was held that Section 280 is silent as to whether a transferee may be assessed where the period of limitation for assessment against the taxpayer expired prior to the enactment of the Revenue Act of 1926, without any assessment against the taxpayer having been made or without a proceeding in court against him having been begun, and consequently under those circumstances they applied the general rule that where the right to assess the tax against the transferor had become barred prior to the enactment of the Revenue Act of 1926, the right to enforce a liability for such tax against the transferee had thereby become unenforcible.

The courts have continued to adhere to the same rule.

United States vs. Snook, 24 Fed. (2d) 844, decided March 5, 1928.

United States vs. Armstrong, 26 Fed. (2d) 227, decided April, 1928.

The Committees of Congress having in charge the formulation of Revenue legislation, continued to recognize the application of Section 278 (d) to transferees and fiduciaries. The limitation provisions in Section 280 were exactly the same as to fidicuiaries of an estate as they were to transferees generally. Consequently, if the provisions of Section 278 (d) were available to fiduciaries upon claims for taxes owing by a deceased, they were likewise available to transferees of the assets of a dissolved corporation. Both in the report of the Committee on Ways and Means of the House of Representatives on the Revenue Act of 1928, dated December 7, 1927, p. 24, and of the Committee on Finance of the Senate on the same act, dated May 1, 1928, p. 32, those committees plainly indicated their understanding and intention that the six year period for collection of such taxes after assessment contained in Section 278 (d) should apply, by the use of the following language, in discussing the effect of Section 280 of the Revenue Act of 1926:

> "Under existing law the Government has six years within which to collect income taxes asssessed against the estate of a decedent and accruing during the lifetime of a decedent, or during the administration of his estate."

As section 278 (d) was the only section which limited the right to collect such taxes to six years, the committees were necessarily referring to that section.

The Revenue Act of 1928 was passed May 29, 1928, and although Section 280 (d) of the Revenue Act of 1926 was amended in some respects (Section 505, Revenue Act of 1928) and an identical section, as amended, was inserted in the new law (Section 311, Revenue Act of 1928) to govern cases arising thereunder, Congress inserted no provisions (in the new Section), or amendments to the old Section indicating any disagreement with the rulings and holdings, supra.

On the contrary, Congress in many instances in the 1928 Act indicated that it understood that all of the provisions relating to limitations, refunds, appeals and many other proceedings available to the taxpayer, wherein the right was specifically given to the "taxpayer" only, were, by the general provisions of Sections 280 (a), quoted above, made, by reference, available to the transferee of the assets of a taxpayer, as well as to the fiduciary of an estate.

In Section 280, Revenue Act of 1926, the specific extension of one year for assessment against a transferee, after the time for assessing the transferor had expired, did not apply to a transferee of a transferee, consequently he might avail himself of the settled and accepted and accepted rulings and holdings that the right to assess a liability for the tax was barred when the right to assess the taxpayer was barred, although the period of limitation against the preceding transferee extended one year beyond the period applicable to the taxpayer. To deny him

this greater benefit the 1928 Act extended the time for assessing him one year beyond the time for assessing the "preceding transferee." (Sec. 311 (b) (2), Rev. Act 1928).

In the enactment of Section 280 in the 1926 Act, Congress intended the procedure outlined in Section 274, respecting the collection of deficiencies against taxpayers generally—which provided for notice to the taxpayer of an intention to assess, with a right within sixty days to appeal to the Board of Tax Appeals—to be exclusive for assessing and collecting the liability of a transferee. (Section 280 (a) and Section 274, Revenue Act 1926). (Report of Committee on Ways and Means to the House of Representatives, dated December 7, 1925, p. 10) (Report of Committee on Finance of the Senate, dated January 16, 1926 —calendar date January 22, 1926—pp. 28, 29 and 30).

(Conference Report to the House of Representatives, dated February 22, 1926, pp. 39, 43 and 44). (Report of Joint Committee on Internal Revenue Taxes, supra, p. 15). (Report of the Committee on Finance of the Senate, dated May 1, 1928, pp. 39 and 40).

As a result numerous proceedings were begun against transferees under Sections 280 and 274, Revenue Act of 1926, which found their way into the Board of Tax Appeals, instead of into the courts. Between the time of the enactment of the Revenue Act of 1926 and the Revenue Act of 1928, the constitutionality of Section 280 was challenged and the section was held unconstitutional in the case of *Owensboro Ditcher & Grader Co. vs. Lucas,* 18 Fed. (2d) 798. Fearing that the Section might ultimately

be held unconstitutional, and that therefore the proceedings begun thereunder would be a nullity and not operate to toll the general statutes of limitations, which were running against the transferees in the cases pending before the Board of Tax Appeals, Section 505, Revenue Act of 1928, was enacted in the hope of thereby suspending the general statutes of limitations against transferees "(* * * if a proceeding in respect of the liability is placed on the docket of the Board, until the decision of the Board becomes final) and for sixty days thereafter."

It is suggested on p. 14 of the Government's brief that by the enactment of Section 604, Revenue Act of 1928, prohibiting suits to restrain the enforcement of the liabilities of transferees under Section 280, Congress indicated an intention to treat the liability of transferees as distinct from the liability of taxpayers, because that action was not necessary if Section 3224 R. S. (U. S. C., Title 26, Section 154), prohibiting the maintenance of a suit for the purpose of restraining the assessment or collection of any tax, was applicable. The facts are that the Department of Justice and Bureau of Internal Revenue had consistently taken the position in numerous court cases that proceedings against transferees were proceedings to collect taxes and that while the transferees were making the contrary contention Section 3224 was applicable.

Owensboro Ditcher & Grader Co. vs. Lucas, 18 F. (2d) 798 (D. C. W. D. Ky.).

Ralston vs. Heiner, Coll., 24 F. (2d) 416 (C. C. A. Pa.).

Felland vs. Wilkinson, 33 F. (2d) 961 (D. C. W. D. Wisc.)

Trinacia Real Estate Co. vs. Clarke, 34 F. (2d) 325 (D. C. N. D. N. Y.).

Mid-Continent Petroleum Corp. vs. Alexander, 35 F. (2d) 43 (D. C. W. D. Okla.).

To settle this controversy by statute, instead of awaiting an opinion of a court of last resort, Congress passed Section 604. When you know what prompted the passage of this Section, it is quite apparent that the inference sought to be drawn by the Government is not justifiable.

In the case of *Felland vs. Wilkinson*, supra, the court used this significant language:

* * *

"It must be borne in mind that while the liability of a transferee may not be a tax liability in the ordinary sense, nevertheless it is a liability for a tax; in other words, the government is seeking to collect what is primarily a tax and continues to be a tax although, because of the inability to collect from the taxpayer proper, it seeks to require his transferee to pay. From the standpoint of the government the money sought in this case is as much an item of revenue as it would be were the proceedings to collect directed toward the Stoughton Lumber Association. * * *

"In this view, it seems that section 604 may and should be given effect according to its terms in the same manner as has section 3224, as a part of the 'system of corrective justice, intended to be complete,' placing the transferee in the same category as a taxpayer in so far as he is required to first pay the tax liability and thereafter seek recovery back."

In the case of *Routzahn vs. Tyroler*, 36 F. (2d) 208 (6th CCA) the Department of Justice and the attorneys for the Bureau of Internal Revenue again took the position that a transferee was a "taxpayer," within the mean-

ing of that "term," as used in Section 1001, Revenue Act of 1926, and Section 1224, Title 26, U. S. C. A., where the right of review of a decision of the Board of Tax Appeals was expressly given only to the "taxpayer", and induced the court to so hold.

The facts in the *Trinacia Real Estate Co. vs. Clarke* case, supra, show that the Bureau of Internal Revenue has in other respects recognized that proceedings against a transferee is a "proceeding to collect a tax," by making jeopardy assessments against a transferee under Section 279, Revenue Act of 1926, which section contains no reference to transferees, but only grants the right to the Commissioner to make jeopardy assessments against the "taxpayer." It further appears from the facts of this case that in the very notices which the Commissioner of Internal Revenue sends out to transferees, in proceedings under Sections 280 and 274, the Commissioner recognizes that such proceedings are for the collection of *"a tax,"* because in the notice sent out therein, which we assume is the standard form, the Commissioner says:

> "In accordance with the provisions of Section 279 (a) of the Revenue Act of 1926, there has been assessed against you income tax, penalty and interest, amounting to $16,502.66, for the taxable years 1920 to 1926, inclusive, as transferee of the assets of Joseph Falcone * * *. As provided in Section 280 of the Revenue Act of 1926, there has been assessed against you the amount of $16,502.66 in taxes,

penalties and interest, constituting your liability as a transferee of the assets of Joseph Falcone * * * for unpaid income taxes, penalties and interest, in the amount of $16,502.66 assessed against Joseph Falcone * * *."

In view of the foregoing, the following rules, announced by this court in *United States vs. Jackson,* (Dec. 5, 1929), as summarized in the syllabus, become pertinent:

"Great weight is properly to be given to the construction consistently given to a statute by the executive department charged with its administration; and such construction is not to be overturned unless clearly wrong, or unless a different construction is plainly required.

"The silence of Congress in the face of a long-continued practice of an executive department involving the construction of a Federal statute must be considered as equivalent to consent to continue the practice."

See also *Brewster vs. Gage,* (Jan. 6th, 1930) wherein the holding is stated in the syllabus, as follows:

"The practical interpretatiton of an ambiguous or doubtful statute that has been acted upon by officials charged with its administratiton will not be disturbed except for weighty reasons.

"The substantial re-enactment in later income tax statutes of a provision theretofore construed by a regulation of the Treasury Department is persuasive evidence of legislative approval of the regulation."

(b).

"If the general statutes of limitation in the Revenue Act of 1926 do not apply to proceedings under Section 280, they should not apply to this proceeding which was not brought under the Revenue Act but was instituted under general equitable principles." (pp. 7, 8, Gov. Brief).

The Government admits that the general statutes of limitation respecting assessments, plus one year, apply to transferees in proceedings under Section 280, and it must be clear that the general statutes of limitation respecting collection are applicable in such proceedings. Using the Government's own argument, we say that if Congress has limited the time within which the Government may proceed against a transferee under Section 280, it is unreasonable to suppose that Congress intended that the Commissioner, by electing to proceed against a transferee in equity, instead of under 280, could thereby deny to him the benefit of the limitation provisions in Section 280, as well as all other limitation provisions, and forever hold against him the claim for taxes.

(c).

The appellees meet the contention of the Government that the so-called trust fund theory enables the Government to treat this proceeding as an independent suit, not to collect taxes, but to recover a trust fund, by the counter contention that this is a proceeding to collect taxes, that it is not an independent suit, that it is ancillary and in the nature of an equitable execution, and entirely dependent upon the continued existence of the original claim as a basis for its maintenance.

Under this heading the Government develops its "trust fund theory," and makes the contention that the

limitations in the revenue acts apply only to taxes "*qua* taxes," and not to assets in equity to recover "trust funds."

To this we make answer that a suit in equity to pursue the assets of a corporation into the hands of its transferees, is an equitable execution and is, therefore, a proceeding "for the collection of taxes," just as this court held in *Bowers v. Lighterage Co.*, 276 U. S. 346, that a "distraint" was a proceeding for the collection of a tax under Section 250 (d) of the Revenue Act of 1921, where the language was "proceeding for the collection of the tax," the word "court" not yet having been inserted in that section. If, under the 1921 Act, distraint by the Collector is a "proceeding" for the collection of a tax, and barred by the provisions of a section which does not place a limitation upon the distraint, then, obviously, by the same reasoning, a creditor's bill against transferees in aid of the collection of a tax, is a "proceeding in court for the collection of a tax" under Section 278 (d) of the Act of 1926, since both processes, that is, the distraint upon the assessment, and a creditor's bill to pursue assets into the hands of a transferee, serve precisely the same purpose.

Russell v. United States, 278 U. S. 181, which the Government brings into its brief and attempts to parry, was a suit against transferees for the enforcement of the claim of the Government for taxes against the transferor. There was no other question in the case, except whether the action was barred by the limitations contained in Section 278 (d) of the Revenue Act of 1924, which, so far as this question is concerned, does not dif-

fer from similar provisions in the section of the 1928 Act, although that later act contains other clauses making it clearly retroactive, whereas, the 1924 Act is held not to be retroactive. But in applying the 1924 Act to the claim in that case, the court throughout assumes that if there is a limitation against the taxpayer, there is also a limitation against the transferee, and the transferee is there given the benefit of the limitations contained in the section. The contention of the Government now is that the case is not in point, because attention was not called to what is now termed the "trust fund theory." Apparently, the Government was not, at the time of the presentation of that case, so greatly impressed with the trust fund theory as its representatives are now, although it is to be noted that when the Russell case was argued to this court on November 22, 1928, this Updike case had been heard and decided in the district court, and the appeal of the Government had been taken to the circuit court of appeals, and was there pending.

The Government also contends that the decision of this court in the case of *United States vs. Barth*, 279 U. S. 370, is in point. But we submit that a decision that a suit upon the bond given by the taxpayer and a surety was, in its very essence, a suit upon a contract. Surely there is a distinction between a suit upon a new and independent contract, no matter what the obligation which furnished the consideration for it, and a suit upon the original claim. But, as we shall see, the suit of the Government in this case is not upon any new promise, but upon the original claim itself.

The liability at law or in equity of a transferee of the property of a debtor terminates when the right to collect from the debtor is barred or extinguished.

As a means of avoiding the effect of the limitations contained in Sec. 278 (d) of the Revenue Act of 1926, as well as of any other limitations in prior acts, which may be applicable to this claim, the Government contends that its suit is a proceeding to distribute trust funds among the beneficiaries of a trust, and a separate and distinct suit from the suit against the taxpayer, and, therefore, not governed by the limitation in that section, and without any limitations, since there must be a specific provision found in the Federal statute to limit suits by the Government.

In the statement of the questions presented on p. 2 of the Government's brief, this proceeding is referred to as a suit in quity, brought under the trust fund theory against the stockholders of a dissolved corporate taxpayer "for money received to the use and benefit of the United States."

In its essence, this suit is a creditor's bill, that is, a suit brought by a creditor against the transferees of the assets of a debtor, to collect from the transferee, not as a liability of the transferee, but simply by pursuing property into the hands of the transferee, a debt claimed to be owing from the transferor.

The issue between the Government and the respondents in this case is not only a question of a separate statute of limitations running in favor of the transferee, or any limitation operating in favor of the transferee,

but whether there is any cause of action of any kind or character at any time against the transferee of the assets of a debtor, unless there is first established a subsisting claim against the transferor, as the necessary foundation of the suit against the transferee.

From the argument of the Government in this case, it would seem that, as a creditor, the Government is no longer concerned with its claim against the taxpayer. It claims, in effect, although this is no where so stated in the Government's brief, but is necessarily deducible from it, that by the distribution of its assets to its stockholders, the Updike Grain Company created a trust for the benefit of the Government, and thereby, of course, discharged its own liability to the Government, and made this money in the hands of the stockholders a trust fund for the use and benefit of the Government, to which the Government may resort for the satisfaction of the claim which it formerly made against the taxpayer, but now, by the necessary logic of the Government's argument, is no longer the obligation of the taxpayer.

That money which ought to have been used by a taxpayer to pay its taxes, but is transferred in fraud of the Government's rights, does not thereby become the money of the Government, has been expressly held and decided by this court, with the sympathy and suggestion of the Treasury Department itself, in the case of *Johnson v. United States,* 268 U. S. 220.

The only time when the assets of a dissolved corporation, transferred to its stockholders, differ in any respect from the transferred assets of an individual

debtor, is when a court of equity has taken over the liquidation of the corporation for the benefit of all creditors and of stockholders. Then, for the first time, the so-called trust fund theory becomes applicable. Before that the assets of an insolvent corporation are not held in trust by the corporation itself for its creditors, in any proper sense of the term, or in any other sense, other than that every debtor owes an obligation to use his property for the discharge of his debts, and this obligation is frequently enforceable by appropriate proceedings in equity, and, in such proceedings, property may be impressed with a trust.

This was distinctly ruled as to Nebraska corporations by the Supreme Court of Nebraska, in *Shaw v. Robinson & Stokes,* 50 Neb. 403, where it was held that the right of a debtor to prefer one creditor over another in the absence of bankruptcy was not affected by the fact that the debtor was an insolvent corporation. Obviously, if property of an insolvent corporation is held in trust, it must be administered as a trust for the benefit of all, and not for one of the beneficiaries.

Treating this suit then as it should be, as a creditor's bill, to collect from the transferee of property, an obligation that ought to have been paid by the transferor, the answer to the question propounded by the Government as an appellee in this case, is not difficult.

It is to be noted that neither the statutes of Nebraska, nor any revenue law or other statute of the United States can be invoked in aid of the liability alleged against these stockholders. Not even Sec. 280

creates any liability against stockholders, it merely offers a remedy for the enforcement "of any liability at law or in equity," which may exist against transferees in favor of the Government. The liability of the transferees must be determined primarily by the law of Nebraska under which this corporation was organized and dissolved, aided, no doubt, by general principles of equity relating to such transactions, and as to these the rulings in Nebraska do not differ from the current of decisions elsewhere.

It is the settled law in Nebraska that before a suit can be brought against the transferees of the property of a corporation, to collect a debt of the latter, the obligation must be reduced to judgment and execution at law issued.

Mer. Nat. Bk. v. McDonald, 63 Neb. 363.

In all of such proceedings it is recognized that a suit against a transferee is ancillary to the principal obligation of the original debtor, and that it can never be enforced unless there is an existing obligation of the original debtor upon which the money collected by the ancillary proceedings may be applied. It is the law of Nebraska, and it is in accordance with the latest ruling of this court upon the subject, even when the Government of the United States is enforcing a claim against an insolvent and dissolved corporation, that it is a necessary prerequisite for the maintenance of the suit in equity against the stockholders, that a judgment at law must be obtained against the principal debtor, and execution issued and returned unsatisfied. *Merchants Nat. Bk. v.*

McDonald, 63 Neb. 363; *Pierce vs. United States,* 255 U. S. 398.

It is said in the latter case, (p. 403):

> "But when a corporation devests itself of all its assets by distributing them among the stockholders, those having unsatisfied claims against it may follow the assets, although the claims were contested and unliquidated at the time when the assets were distributed. It is true that the bill to reach and apply the assets distributed among the stockholders, cannot, as a matter of equity jurisdiction and procedure, be filed until the claim has been reduced to judgment and the execution thereon has been returned unsatisfied (*Hollins v. Brierfield Coal & I. Co.,* 150 U. S. 371.)"

> "A judgment creditors bill is in essence an equitable execution." (p. 402)

The formality of obtaining a judgment and having execution issued against the insolvent debtor may well be waived by the transferee in a suit brought against him, or its necessity may be abolished by statute. *McWilliams vs. Excelsior Coal & I. Co.,* 298 Fed. 884.

But in any case, whether the judgment at law is obtained, or proceedings directly against the transferees are authorized or permitted, the essential nature of the proceeding remains the same. It is still ancillary to the main claim which must be established if disputed, either by a judgment at law or in the equity suit in which relief is sought.

Porter vs. Wingert, 200 Ia. 1371;

Cunningham vs. City of Cleveland, 98 Fed. 657;

Houghton vs. Axelsson, 64 Kans. 274;

Pierce vs. United States, 257 Fed. 514;

A creditor's suit is so dependent upon the prior suit to recover judgment upon the debt, that the courts of the United States have jurisdiction of such suits, although between citizens of the same states, if the original action in which the judgment was obtained had the requisite diversity of citizenship. *New Orleans v. Fisher,* 180 U. S. 185; *Hatcher v. Hendric,* 133 Fed. 267; *Dewey v. Coal Co.,* 123 U. S. 329; *Campbell v. Min. Co.,* 141 Fed. 610.

Proceedings to collect from a transferee, a claim or obligation of its transferor, are always ancillary to the principal claim, and can never arise above their source, and can not be pressed after the principal obligation has ceased to exist.

This proposition is so well understood in the law that it has been enforced in various ways. It is well settled that if the claim or judgment against the principal debtor becomes barred by limitation or otherwise, even while the ancillary proceedings are pending in court, the result is to terminate the right to prosecute the ancillary proceedings.

A leading case on this proposition is *Dole vs. Wilson,* 39 Minn. 330, where the court said:

> "The plaintiff is seeking, through the equitable jurisdiction of the court, to have this land appropriated to the satisfaction of his judgment after the judgment itself has expired by lapse of time. Equity will regard the statutory limitation upon the life and enforcibility of the judgment, and will not inter-

fere to enforce its satisfaction by means of its peculiar remedies; thus avoiding the effect of the statutory limitation, if by the plaintiff's own neglect, the judgment has been suffered to remain unsatisfied until it has ceased to exist as a legal obligation.

And with respect to the contention that the assets in the hands of the transferee were a trust fund, the court said:

> "The plaintiff contends that the lapse of time has not prejudiced the right of action here asserted, because, upon the facts alleged, the law implies and declares a trust in favor of creditors, as respects the land in question. The rule exempting cases of trust from the operation of statutes of limitation is not applicable to resulting trusts of this nature, which do not involve the peculiar confidential relations generally subsisting between trustees and *cestuis que* trust."

In *Flagg vs. Flagg,* 39 Neb. 229, the Supreme Court of Nebraska held that while proceedings were pending in equity to enforce a judgment, which became dormant while the suit was pending, upon that fact being called to the attention of the court by supplemental answer, the proceedings in equity must be dismissed and the claim of the judgment creditor denied.

This appears to be the general rule except where controlled by special statute. *Holmes vs. Webster,* 98 Neb. 105; *Fisher vs. Woodard,* 103 Neb. 253; *Newell vs. Dart,* 28 Minn. 243; *Bank vs. Braithwaite,* 7 N. D. 352; *McAleer vs. Clay County,* 42 Fed. 665; *Board of Commissioners vs. Tome,* 153 Fed. 81; *General Electric Co. vs.*

Hurd, 171 Fed. 984; *Mullen vs. Hewitt,* 103 Mo. 639; *Scott vs. Neely,* 140 U. S. 106.

In the case last cited, the court said:

> "In all cases where a court of equity interferes to aid the enforcement of a remedy at law, there must be an acknowledged debt or one established by a judgment rendered, accompanied by a right to the appropriation of the property of the debtor for its payment."

There is no analogy between this case and the cases cited by government counsel where the statutory limitation against a suit by the government to annul a patent for public lands, did not operate as a bar to a suit by the government to recover the value of lands, where the patent had been procured by fraud.

At pages 12, 45 and 59 of the Government's brief, reference is made to the case of *United States vs. Whited & Wheless,* 246 U. S. 552, and other similar cases wherein it was held that the statute of limitations expressly applicable to suits by the Government to annul a patent for public lands, was not applicable to suits to recover the value of the land, on the ground of fraud in procuring the patent.

The important distinction between the two cases arises from the fact that in the case of the public lands, the suit to recover the value of the land is in no sense subordinate or ancillary to the suit to annul the patent. Upon the contrary, it is an alternative and an entirely independent proceeding, and it has been held in subsequent decisions that the Government must elect whether it will avail itself of one remedy or the other, and

having made its final election, it has thereby lost the other remedy. *United States vs. Oregon Lumber Co.*, 260 U. S. 290.

But in *Pierce vs. United States*, 255 U. S. 398, where it was contended that a suit against a transferee of assets of a corporation could not be maintained, because the Government had prosecuted a suit in another jurisdiction to enforce an agreement made by the transferee of the assets, it was held that such action did not amount to an election of remedies which would bar the Government from following by creditors' bill the assets of the judgment debtor in the hands of its stockholders. The suit against the purchaser did not amount to an election of remedies which should have defeated the creditors' bill against the stockholders.

Of course, it is familiar practice that in efforts to collect a judgment at law, one creditors' bill may follow another, or both may follow several executions or other proceedings claiming a right to collect a debt in some other jurisdiction, without any question ever arising as to election of remedies.

It is to be noted that the Government cites no cases whatever in support of its proposition that the creditor's suit against the transferee may be prosecuted independently of the existence of a continuing liability on the part of the taxpayer.

In the brief, at pp. 23, 24 and 25, and subsequent pages, there is an argument to the effect that a suit against the stockholders of a corporation to recover from

them a debt originating with the corporation, is a distinct suit, and governed by separate statutes of limitation and separate procedure.

It is unfortunate that most of the cases on which the Government relies in this discussion are not suits to recover a debt of the corporation out of assets transferred by the corporation to its stockholders, but are cases in which the creditor was relying upon a statute relating to a separate and independent liability on the part of stockholders for the corporation's debts, either because of an unpaid subscription to the capital stock, or on the double liability of stockholders, created by both state and Federal statutes, or a liability upon stockholders because of some failure to comply with the statutes relating to corporations. Those cases have no application to this discussion. Thus, in *Bourne v. Baer,* 107 Neb. 255, cited at p. 27 of the Government's brief, the liability there asserted was upon two grounds, one to recover unpaid subscriptions to the capital stock, and the other to recover from the stockholders the amount of the debt of the corporation as a penalty arising from the failure of the officers to cause notice of indebtedness to be published, as required by the state statute. There was no question in this case of pursuing the transferred assets of a corporation. So, in *McDonald v. Thompson,* 184 U. S. 71, cited on p. 25 of the Government's brief, the action was by a receiver of a national bank to recover the liability imposed by statute, and not for the recovery of transferred assets.

In *Whitman v. Oxford National Bank*, 176 U. S. 559, also cited on p. 25 of the Government's brief, the action was to recover on a statutory liability of stockholders of corporations organized under the laws of Kansas.

Case vs. Beauregard, erroneously cited as in 101 U. S. 688, but actually found in the original decision in 99 U. S. 119, where it appears that the suit was against the assets of a partnership, in no manner involves the question we are discussing.

The later case of *Case vs. Railroad Co.*, 101 U. S. 688, merely held that the decision in the first case constituted an adjudication of the issues tendered by the second. In any case, there was no question about following the transferred assets of a dissolved corporation.

Terry v. Anderson, 95 U. S. 628, cited on pp. 24 and 25 of the Government's brief, was a suit on the unpaid subscription of the stockholders of a bank, and had nothing to do with transferred assets.

As to the cases cited by counsel at the beginning of p. 23 of Government's brief, being the early decisions of this court that are assumed to be the foundation of the adoption of the trust fund doctrine, it is, of course, sufficient to say that they are not controlling as against the decisions of this court in the later cases cited on the same page. But even the earlier decisions are all consistent with the present doctrine of the assets of corporations, since they merely held that a creditor of an insolvent or dissolved corporation, is not by reason of the dissolu-

tion barred from enforcing his claim at all, as was the case at common law, but that he is entitled to collect his debt out of such of the assets of the corporation as have not passed into the hands of a purchaser for value. Not all of these cases discuss the procedure by which the claim may be satisfied, and they are all consistent with the theory that the remedy of a creditor of a corporation is exactly the same as the creditor of an individual as to transferred assets.

In *Mumma v. Potomac Co.*, 8 Pet. 281, the only holding was that under the local law affecting the corporation, the corporation, after its dissolution, could not be sued, nor could a former judgment against it be revived by *scire facias*. It was suggested by the court that the creditor was not without remedy, since he could enforce his claim against any assets of the corporation which had not passed into the hands of purchasers, and the only trust apparent in that case was one specifically created by the statute creating the corporation.

In *Railroad Co. v. Howard*, 7 Wall. 392, the holding merely was that where a court of equity takes possession of the assets of a corporation to foreclose a first mortgage on it, it will retain any surplus proceeds from the sale, and administer it as a trust fund for the payment of other creditors. This is also quite consistent with the later holdings on the subject.

In *Curran v. Arkansas*, 15 How. 304, the plaintiff was a creditor of an insolvent banking corporation, created under the laws of Arkansas, and which, by later enactments, was dissolved and its assets transferred to the

state of Arkansas itself. The court held that creditors of the bank could pursue the assets into the hands of the state and recover them. This was by a divided court, three justices dissenting.

In *Sanger v. Upton,* 91 U. S. 56, the suit was to recover unpaid subscriptions to the capital stock, and the decision seemed to have no bearing upon the issues here.

In *Swan vs. Frank,* 148 U. S. 603, the holding was that a creditor could not pursue the transferred assets of a dissolved corporation, because he had not obtained a judgment against the corporation. There is one dissenting opinion holding that in that particular case a judgment could not have been obtained, and, therefore, the action ought to be maintainable.

2.

The Government on page 29 of its brief states its contention as follows:

> **"Even though it should be conceded that the defense of a statute of limitations relating to the collection of taxes was available to the respondents, such defense fails in this case for the reason that the returns required by law have not been filed, without which no statute of limitations has been set in motion."**

We challenge the contention that returns were not filed, and will discuss that, *infra,* but will concede that contention for the purposes of this portion of the brief.

The point made by the Government under this portion of its brief is that the taxpayer filed no return for the fiscal period involved; that under Section 278 (a) the tax could be assessed, or a proceeding in court for

the collection of such tax, without assessment, could be begun at any time, and that, therefore, when the tax was assessed in January, 1920, it was not assessed "within the statutory period of limitation properly applicable thereto." In other words, it is said that the period for the assessment of a tax, where no return has been filed, is "at any time," but because "at any time" is an unlimited period, it cannot therefore be a period of limitation. A mere quibble over words and phraseology to defeat the plain intent of Congress, which is plainly indicated in a comparison of the 1926 Act with the 1924 and prior Revenue Acts, and in the proceedings and reports of the committees of Congress, when the 1926 Act was under consideration.

Fortunately for the respondents the word "period" has been given a statutory definition or construction in the Revenue Act of 1924, which, undoubtedly, Congress had in mind and adopted when it drafted Section 278 (d) of the 1926 Act. Section 278 (a) of the 1924 Act is the same as Section 278 (a) of the 1926 Act.

In Sub-division (d) of the 1924 Act, it is provided:

> "Where the assessment of the tax is made within the period prescribed in Section 277 or in this Section, such tax may be collected by distraint or by a proceeding in court, begun within six years after the assessment of the tax."

When we look for "the period pres bed * * * in this Section," we find that the only "period prescribed" is "at any time."

The word "period" was likewise given the same statutory definition, interpretation or construction in another part of the 1924 Act. In Section 1009 (b) of that Act, it is provided:

> "In case of a false or fraudulent return with intent to evade tax, or a failure to file a required return, or of a willful attempt in any manner to defeat or evade tax, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

In Sub-division (c) of the same Section, it is provided:

> "Where the assessment of the tax is made within the period prescribed in subdivisions (a) and (b) such tax may be collected by distraint, or by a proceeding in court, begun within six years after the assessment of the tax. Nothing in this Act shall be construed as preventing the beginning, without assessment, of a proceeding in court for the collection of the tax at any time before the expiration of the period provided in subdivision (a) for the beginning of such proceeding."

As there was no other "period prescribed" in Subdivision (b) than "at any time," Congress could only have intended that "period" should mean "at any time."

No such narrow, strained or forced construction or interpretation has been indulged in by the Government when its interests required a contrary construction, because in the following General Counsel's Memoranda and Rulings it has been determined that the phrase "statutory period" as used in Section 278 (d) of the Revenue Act of 1926, means the statutory period plus any additional

time extended by waivers, even though the waivers were unlimited as to time.

G. C. M. 2513, Ruling VI-45-3496.

G. C. M. 2939, Ruling VII-6-3597.

G. C. M. 2408, Ruling VI-41-3461.

In *Atkins vs. Bender,* 26 Fed. (2d) 690, (D. C. W. D. La.), the court adopted the same view.

It might also be helpful in arriving at the intent of Congress with respect to the effect of subdivision 278 (d) of the Revenue Act of 1926 to note that in Sec. 250 (d) of the Revenue Act of 1921, it is provided:

> "That in the case of a false or fraudulent return with intent to evade tax or of a failure to file a required return, the amount of tax due may be determined, assessed and collected and a suit or proceeding for the collection of such amount may be begun at any time after it becomes due."

In the 1924 and 1926 Acts, Section 278 (a) is as follows:

> "In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun *without assessment,* at any time."

It will be noted that in the 1921 Act, the two separate remedies of assessing at any time, and of a suit or proceeding at any time, are cumulative and there is no restriction on the conditions for bringing the suit or proceeding. In the 1924 and 1926 Acts, the two remedies are given in the alternative, the tax may be assessed, "or"

a proceeding in court for the collection may be begun "without assessment" at any time.

If the Acts of 1924 and 1926 have the construction contended for by the complainant in this case, that is, that there is never any limit on a suit to recover the tax after it has been assessed, then there is no reason why Congress should have made any change in that respect from the 1921 Act, since that had been construed to mean just what the complainant contends the later acts mean. Congress must have had some purpose in changing the language. Subdivision (a) in Sec. 278 in the later acts places no limit on the time within which the tax may be assessed and places no limit on the time within which a proceeding in court may be begun for the collection of the tax "without assessment." But it obviously left open for further treatment any limitation which Congress intended to make on the collection of a tax after an assessment had been made. This is found in subdivision (d) of Sec. 278 of the two acts. These differ from each other, but properly construed they both mean substantially the same, except that the 1924 Act uses the language "within the period prescribed in Sec. 277 or in this section," whereas the 1926 Act uses the language "within the statutory period of limitation properly applicable thereto;" thus indicating that where the 1924 Act applies only to assessments made, as prescribed in Sections 277 and 278 of that Act, yet the 1926 Act was not so limited, but will apply to an assessment made anywhere, at any time, under any section of any act.

It should also be noted that in the 1924 Act and prior Acts, when reference is made to statutes of limitation

contained in some of the sections, the specific sections were referred to, but, in the 1926 Act a definite policy was adopted and adhered to, by the uniform use of the expression "within the statutory period of limitation properly applicable thereto," instead of by reference to the particular sections containing such limitations.

No one can review the history of income tax legislation during the ten years preceding the passage of the 1926 Act, without reaching the irresistible conclusion that Congress intended in both the 1924 and 1926 Acts to put a time limit upon the collection of old taxes in all cases where the Government had become cognizant of the fact that a tax was owing.

Beginning with the Revenue Act of 1918, it has, in each successive act, put a time limit upon both the assessment and collection of income, war-income, and excess-profits taxes, in all cases where a substantially correct return had been filed, regardless of whether the return correctly stated the net income or not.

Section 250 (d) of the Revenue Act of 1918.

Section 250 (d) of the Revenue Act of 1921.

Section 1322 of the Revenue Act of 1921.

Section 1320 of the Revenue Act of 1921.

Section 277 (a) (2) of the Revenue Act of 1924.

Section 277 (a) (3) of the Revenue Act of 1926.

Section 1109 (a) (1), (2), (3) of the Revenue Act of 1926.

As early as the Revenue Act of 1916, the taxpayer who failed to file a return, or who even filed an erroneous,

false or fraudulent return, was relieved from an assessment if the Government did not discover that fact within three years after the return was due.

Section 14 (a) of the Revenue Act of 1916.

In the 1918 Act, a five year limitation applied to both the assessment and collection of taxes against persons who failed to file a return, and the limitation period started to run from the date the return was *"due."*

Section 250 (d) of the Revenue Act of 1918.

In the Revenue Act of 1921, a four year limitation upon the assessment and a five year limitation upon proceedings to collect was prescribed with respect to all internal revenue taxes not specifically covered by other limitation provisions in the Act. The period of limitation started to run from the time the tax was *"due"* in every case where the taxpayer acted in good faith, and only excepted cases where there was fraud "with intent to evade" tax or a "wilful" attempt to defeat or evade the tax.

Sections 1320 and 1322 of the Revenue Act of 1921.

In the 1924 and 1926 Revenue Acts, limitations of four years in some instances and five years in others were prescribed for both the assessment and collection of the tax, and even protected a taxpayer who had filed a false or fraudulent return, if he did so without intent to evade tax.

Sections 277 (a) (2) and 278 (a) of the Revenue Act of 1924.

Sections 277 (a) (3) and 278 (a) of the Revenue Act of 1926.

In the 1921 Act, Congress first coupled together in the limitation provisions the person who filed a false or fraudulent return with the person who failed to file a return, making the period of limitation for both the assessment and collection of the tax "at any time;" but in the case of the person who filed a false or fraudulent return, there was a limitation of five years unless such person did so with an "intent to evade tax," while in the case of a person who failed to file a return, no amount of good faith or good intent permitted him to avail himself of the lesser limitation period. The reason for this advantage to the person filing a false or fraudulent return over the person who, in the utmost good faith failed or neglected to file a return, has nowhere and at no time been explained, and seems indefensible.

Section 250 (d) of the Revenue Act of 1921.

In the 1924 and 1926 Acts, the time for the assessment of the tax in the two cases named above remained the same as in the 1921 Act, to-wit: "at any time;" but a six year limitation was placed upon proceedings for the collection of the tax, after an assessment had been made; starting to run from the date of the assessment of the tax. That time was undoubtedly adopted, (as will be shown, infra, from the proceedings before the Committee on Finance of the Senate,) because Congress did not wish any statute of limitations to run against the Government in those instances, until after the Government had acquired knowledge of the obligation for the tax. The assessment of a tax both settled the question of the knowledge of the

Government, and furnished a definite date for the beginning of the limitation period.

In construing limitation provisions in a tax law, we must keep in mind that they are not limitations upon the enforcement of some Government claim arising out of some contract or tort obligation where the conduct of the debtor has been involved in the creation of the obligation, but are limitations upon a statutory obligation created by the arbitrary and *ex parte* action of the Government in the exercise of its taxing powers.

The Government must and can look only to its statutes for the obligation it has thus created, and there is no odium attaching to the citizen who points to the same statute for a termination of the obligation.

In the case of *Wood vs. Carpenter,* 101 U. S. 135, it is said:

> "Statutes of limitation are vital to the welfare of society and are favored in the law. They are found and approved in all systems of enlightened jurisprudence. They promote repose by giving security and stability to human affairs. An important public policy lies at their foundation. They stimulate to activity and punish negligence. While time is constantly destroying the evidence of rights, they supply its place by a presumption which renders proof unnecessary. Mere delay, extending to the limit prescribed, is itself a conclusive bar. The bane and antidote go together."

By reason of the arbitrary nature of tax laws, they are strictly construed against the Government and liberally construed in favor of the taxpayer, and the same rule

of construction applies to the limitation provisions in tax laws.

In the recent case of *Bowers, Collector of Internal Revenue vs. New York & Albany Lighterage Co.,* 273 U. S. 346, 47 S. Ct. Rep. 389, this court, in construing a limitation provision in the Revenue Act of 1921, said:

> "Taxing laws are to be interpreted liberally in favor of the taxpayer. (Syllabus.)
> * * * * * *
>
> "The question for decision is this: Where, under the tax laws enacted prior to the Revenue Act of 1921, income and excess profits taxes were assessed within five years after filing return, does Sec. 250 (d) of that act bar collection by distraint proceedings begun after the expiration of the five-year period?
>
> "The part of the subdivision that has a bearing is printed in the margin. The clause in controversy is: 'No suit or proceeding for the collection of any such taxes . . . shall be begun, after the expiration of five years after the date when such return was filed.' Petitioner insists that the word 'proceeding' refers only to a proceeding in court and means the same as 'suit;' and that the act prescribes no limitation against the collection of such taxes by distraint.
> * * * * * *
>
> "He maintains that any ambiguity in the clause under consideration must be resolved in his favor. Undoubtedly the United States will not be held barred by a general statute of limitation unless, upon a strict construction in its favor, the United States and the claim sought to be enforced fairly may be held to be within the terms and purpose of the statute. *E. I. Dupont de Nemours & Co. vs. Davis,* 264 U. S. 456, 462, 68 L. Ed. 788, 791, 44 Sup. Ct. Rep. 364. That rule rests upon the general principle of policy applicable to all governments that the public interest should not be prejudiced by the default or negligence

of public officers. *United States v. St. Paul, M. & M. R. Co.*, 247 U. S. 310, 314, 62 L. Ed. 1130, 1132, 38 Sup. Ct. Rep. 525. The limitation applies to petitioner and to the claims. It applies to suit; the only question is whether it also bars distraint. The provision is a part of a taxing statute; and such laws are to be interpreted liberally in favor of the taxpayers. *Eidman v. Martinez*, 184 U. S. 578, 583, 46 L. Ed. 697, 701, 22 Sup. Ct. Rep. 515; *Schwab v. Doyle*, 258 U. S. 529, 536, 66 L. Ed. 747, 753, 26 A. L. R. 1454, 42 Sup. Ct. Rep. 391.

* * * * * *

"The provision is to be applied in harmony with the intention reasonably to be inferred from its terms and the circumstances of its enactment. *Cf. United States v. Oregon Lumber Co.*, 260 U. S. 290, 299, 67 L. Ed. 261, 270, 43 Sup. Ct. Rep. 100. Prior to the Revenue Act of 1918 there was no limitation against suit to collect income taxes. Section 250 (d) of that act (February 24, 1919) 40 Stat. at L. 1083, chap. 18, Comp. Stat. Sec. 6336, Fed. Stat. Anno. Supp. 1919, p. 115) required assessment within five years after return, and prohibited the commencement of suit or proceeding to collect such taxes after that period. This bar was held to apply only in respect of taxes for 1918 and later years. Then Sec. 250 (d) of the Act of 1921 made the limitation apply against collection of taxes under all the earlier acts; and, in pursuance of a legislative purpose to require more prompt action upon the part of the commissioner and collectors, prescribed the five-year period for determination and assessment of taxes under earlier acts, but allowed only four years as to those for 1921 and succeeding years. The same purpose is shown by the requirement that the commissioner, within one year after request by their personal representatives, shall make assessments on income received by deceased persons. These stricter limitations applicable to taxes for the later period make against the petitioner's contention that the act sets no bar against collection by

distraint. A reasonable view of the matter is that it was the intention of Congress by the clause here in question to protect taxpayers against any proceeding whatsoever for the collection of tax claims not made and pressed within five years."

We do not need to resort to statutory enactments alone to ascertain the intention of Congress in this respect, because it was made quite plain by Mr. A. W. Gregg, then General Counsel of the Bureau of Internal Revenue, at the hearings before the Committee on Finance of the Senate upon the Revenue Act of 1924, in considering the effect of these provisions as they appeared in Section 1009 (b) and (c) of that Act, quoted, supra, and which are identical with Section 278 (a) and (d) of the same Act, and also as they appeared in Section 278. We set forth the substance of the proceedings as they appear on pp. 39, 40, 41, 49, 50, 51 and 52.

Section 278 (d) of the 1924 Revenue Bill, as it came to the Senate from the House, provided "Where the assessment of the tax is made within the period prescribed in Sec. 277 or in this section, such tax may be collected at any time by distraint or by proceeding in court * * *." In considering this sub-section a discussion arose between Mr. Gregg and various senators (pp. 39-41) as to whether or not there should be a time limit upon the right to collect after an assessment had been made and not leave the time within which the Government may collect open forever, by the use of the phrase "at any time." Action thereon was deferred, but several days later the Committee took up for consideration Section 1009 (b) and (c) of the bill, which was in identical language in that

respect with Section 278 (a) and (d). In that discussion (pp. 49-52) several senators insisted that after the Government had made an assessment there should be a limit upon the time within which it might proceed to collect. Thereupon the question arose as to whether this should apply to fraud cases and no return cases, when the following colloquy took place:

"Senator King (interposing). You distinguish between cases where a return is filed and where there is no intent to deceive and cases where a man delibrately files no return?

"Mr. Gregg. Yes, sir.

"Senator King. In the first instance you were put on notice and you can inquire and ascertain whether there have been any omissions in the return. In the second instance you have not been put on notice, and your contention is that you should have an indefinite period within which to make your assessment. But do you not think in the latter case, after you have made the assessment, there ought to be a limitation within which you may prosecute to a successful issue your claim for the tax?

"Mr. Gregg. * * * There are cases occasionally where we find a taxpayer has failed to file a return, but sometimes we can not prove deliberate fraud. It seems to me that the statute should not begin to run against the Government until the Government is put on notice in a case of this kind.

"Senator Reed of Pennsylvania. The only offenses against which there are no statute of limitations are murder and treason. Why should we class this offense with those two?

"Mr. Gregg. This is not a penalty for the offense; this is for the collection of the tax. There is a statute of limitations on the criminal penalties.

"Senator Reed of Pennsylvania. This is not a thing that I would debate at any length.

* * * * *

"Senator King. As far as I am concerned, if they put in a provision that, after having made the assessment, there will be a period of limitation of 10 years within which they must prosecute to a successful conclusion—

"Senator Jones of New Mexico (interposing). I think six years would be all right.

"The Chairman. Turn to page 177 of the bill and let us fix both of them at the same time.

"Mr. Gregg. Page 177, line 15, strike out the words 'at any time' and insert 'within six years after the assessment.'"

This intention of Congress to put a limitation of six years upon proceedings for the collection of taxes assessed in those cases where no return had been filed, was again evidenced by the interpretation placed upon Section 278 (d) of the Revenue Act of 1926, when that subdivision was up for discussion before the Senate, after that section, as it appeared in the 1924 Act, had been rewritten by the Senate Finance Committee to make it retroactive, in the language in which it appeared in the 1926 Act as passed.

It has been heretofore shown that "fraudulent return" cases and "no return" cases are coupled together in the same limitation provisions of Section 278, consequently whatever limitation provisions applied to "fraud" cases would necessarily apply to "no return" cases.

Section 278 (d) came up for discussion on the floor of the Senate on February 5th, 1926, after being reported

as re-written by the Senate Finance Committee, when the following colloquy took place between Senator King of Utah and Senator Reed of Pennsylvania, ranking member of the Senate Finance Committee to the Chairman, and in charge of the bill on the floor of the Senate at the time:

"Mr. Reed of Pennsylvania. Now, Mr. President, I ask consideration of the committee amendment at the bottom of page 137.

"The Vice President. The amendment will be stated.

"The Chief Clerk. On page 137, after line 23, the Committee on Finance proposes to strike out:

"(d) Where the assessment of the tax is made within the period prescribed in section 277 or in this section, such tax may be collected by distraint or by a proceeding in court, begun (1) within six years after the assessment of the tax, or (2) at any time prior to the expiration of any period for collection agreed upon in writing by the commissioner and the taxpayer.

"(e) This section shall not affect any assessment made, or distraint or proceeding in court begun, before the enactment of this act, nor shall it authorize the assessment of a tax or the collection thereof by distraint or by a proceeding in court (1) if at the time of the enactment of this act such assessment, distraint, or proceeding was barred by the period of limitation then in existence, or (2) contrary to the provisions of subdivision (a) of section 274.

"And in lieu thereof to insert:

"(d) Where the assessment of any income, excess-profits, or war-profits tax imposed by this title or by prior act of Congress has been made (whether before or after the enactment of this act) within the statutory period of limitation properly applicable

thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the commissioner and the taxpayer.

"(e) This section shall not bar a distraint or proceeding in court begun before the enactment of the revenue act of 1924; nor shall it authorize the assessment of a tax or the collection thereof by distraint or by proceeding in court (1) if at the time of the enactment of this act such assessment, distraint or proceeding was barred by the statutory period of limitation properly applicable thereto, unless prior to the enactment of this act the commissioner and the taxpayer agreed in writing thereto, or (2) contrary to the provisions of subdivision (a) of section 274 of this act.

"Mr. King: That relates to fraud, does it not?

"Mr. Reed of Pennsylvania: Yes.

"The Vice-President: The question is on agreeing to the amendment.

"The amendment was agreed to."

(Volume 67, No. 43, Congressional Record, 69th Congress, First Session dated Friday, February 5th, 1926, page 3,068).

That the Bureau of Internal Revenue so interprets Subdivision (d) of the Revenue Acts of 1924 and 1926 is shown in an opinion of Mr. C. M. Charest, General Counsel of the Bureau of Internal Revenue, known as G. C. M. 2939, Int. Rev. Bull. VII-6-3597, promulgated February 6, 1928, wherein, in discussing the difference in the time

limit for the "assessment," from the time limit for the "collection" of income taxes after assessment, he said:

> "The Revenue Act of 1924, enacted June 2, 1924, provided in section 278:
>
> "(d) Where the assessment of the tax is made within the period prescribed in section 277 or in this section, such tax may be collected by distraint or by a proceeding in court, begun within six years after the assessment of the tax. * * *
>
> "(e) This section shall not (1) authorize the assessment of a tax or the collection thereof by distraint or by a proceeding in court if at the time of the enactment of this Act such assessment, distraint, or proceeding was barred by the period of limitation then in existence, or (2) affect any assessment made, or distraint or proceeding in court begun, before the enactment of this Act.
>
> "To the same effect is section 278 (d) and (e) of the Revenue Act of 1926.
>
> "Thus it is apparent that for every case within the purview of the Revenue Act of 1924 a six-year collection period attached after the assessment was made, this regardless of whether the assessment was made before or after the enactment of the Act. (In re *McClure Co., Bankrupt,* 21 Fed. (2d) 538, T. D. 4097 (Internal Revenue Bulletin VI-43, 7); *U. S. v. Crook,* 18 Fed. (2d) 449, certiorari denied by United States Supreme Court October 17, 1927). This holding is based on the general rule of law that a change in the statute of limitations operates to change the period of enforcement of existing causes of action as well as of those accruing thereafter. (*Sampeyreac v. U. S.,* 7 Peters 222; *Sohn v. Waterson,* 17 Wallace 596; *Crothers v. Edison Electric Co.,* 149 Fed. 606)."

Tax laws, like other laws, must be given a reasonable and sensible construction and interpretation, and also a

construction and interpretation that will carry out the obvious intent of the law makers.

Bowers, Collector vs. N. Y. & Albany Lighterage Co., supra.

In *Cohn & Sons Co. v. Commissioner,* 9 B. T. A. 87, a tax case, it is said:

> "Statutes should receive a sensible construction, such as will effectuate the legislative intention, and avoid, if possible an unjust or absurd construction."

Reverting again to facts that obviously disclose the intent of the makers of the Revenue Act of 1926 with respect to Section 278 (d) of that Act, we once more call attention to the fact that the Bureau of Internal Revenue has always construed Section 278 (d) of the Revenue Act of 1924 as applying to assessments made in cases where no return had been filed, and as they were advising the committees having in charge the passage of the 1926 Act, of course so advised those committees.

In the 1926 Act, as originally drafted, and as reported by the Committee on Ways and Means of the House to the House of Representatives, under date of December 7th, 1925, no change had been made in the first sentence of Section 278 (d) as the same appeared in the 1924 Act. In describing the scope of that Sub-division in said report, it is said under the heading,

"Suits to Collect Tax":

"Section 278 (d).

"Sub-division (d) provides that where an assessment of tax is made such tax may be collected by distraint or proceeding in court begun within six years of the assessment of the tax or at any time prior to the expiration of any period for collection agreed upon in writing by the commissioner and the taxpayer."

(See page 12 of Report No. 1 of the Committee on Ways and Means of the House of Representatives on House Rule No. 1, dated December 7th, 1925.)

In fact, when the "Managers on the Part of the House" made the report of the Conference Committee to the House after the bill had passed the Senate with Sub-division (d) re-written as aforesaid, they said:

"Amendment No. 85: This amendment rewrites in more definite language, and correcting clerical mistakes, subdivisions (d) and (e) of section 278 of the House bill, dealing with the time within which distraint or proceeding in court may be begun after the assessment has been made. The House recedes."

(See page 42 of Conference Report to House of Representatives No. 356 accompanying House Roll No. 1 dated February 22, 1926).

That it is proper for this court to consider the above matters in arriving at the intent of Congress, we refer to the following cases:

St. P. M. & M. R. Co., 247 U. S. 310;

Ex Parte Williams, 297 U. S. 267.

Applying the rules of statutory construction and interpretation applicable to all statutes compels the conclusion for which the respondents contend. When coupled with the rule of liberal construction governing taxing statutes for the benefit of the taxpayer, the defendants' contention can admit of no doubt.

II.

Was the collection of the sum sought to be recovered herein from the defendants, as transferees of the assets of Updike Grain Company, barred by sections 250-d of the Revenue Act of 1921, and 277 (a) (2) of the Revenue Act of 1924?

This question calls for an examination of the record to ascertain if returns were filed for the Updike Grain Company, which started the running of the limitation provisions in Sections 250 (d) of the Revenue Act of 1921, 277 of the Revenue Act of 1924, and 277 of the Revenue Act of 1926, which all relate to those cases where returns were filed.

Omitting the inapplicable provisions, these Sections are as follows:

Section 250 (d)—Revenue Act of 1921. (42 Stat. 265)

> "The amount of income, excess profits, or war profits taxes * * due under any return made under this act for prior taxable years or under prior income, excess profits, or war profits tax acts, * * shall be determined and assessed within five years after the return was filed, * *; and no suit or proceeding for the collection of any such taxes due under this act or under prior income, excess profits, or war profits tax acts, * * shall be begun, after the expiration of five years after the date when such return was filed, * * *."

Section 277 (a) (2)—Revenue Act of 1924. (43 Stat. 299)

> "The amount of income, excess profits, and war profits taxes imposed by * * the Revenue Act of 1917, * * and by any such act as amended, shall be assessed

within five years after the return was filed, and no proceeding in court for the collection of such taxes shall be begun after the expiration of such period."

Before reviewing the record with respect to the returns which were filed of the income of the Updike Grain Company, covering that part of the fiscal period of said company in the year 1917, in question here, it should be kept in mind that under the laws and regulations existing up to the time the assessment of the additional tax was made in the instant case, there were three methods of making returns upon which the tax in question in this case might be assessed, viz:

(a) By the taxpayer.

(b) By the Commissioner of Internal Revenue.

(c) By a collector or deputy collector of Internal Revenue.

It is not claimed that a return was made of the income involved herein by a collector or deputy collector of Internal Revenue. We can, therefore, disregard (c).

Statement of the Record Respecting Filing of Returns.

Prior to 1917, the Updike Grain Company was doing business upon a fiscal year basis and had fixed its fiscal year to terminate upon the 31st day of July. In 1917 it duly designated June 30 as the end of its fiscal year.

Under the laws and regulations then existing, the Updike Grain Company, hereinafter referred to as "company," was required to make its return for the fiscal period ending June 30, 1917, on or before August 29, 1917. The Commissioner of Internal Revenue was re-

quired to make the assessment within 90 days after the due date of the return, to-wit: On or before November 28, 1917 (Sec. 14-a, Revenue Act of 1916), except in cases of refusal or neglect to make such return, and in cases of erroneous, false or fraudulent return, in which cases the law provided that "the Commissioner of Internal Revenue shall, upon the discovery thereof, at any time within three years from the date when said return is due, make a return upon information obtained as provided for in this title, or by existing law; and the assessment made by the Commissioner of Internal Revenue thereon shall be paid by such corporation * * * immediately upon notification of the amount of such assessment." (Sec. 14-a, Revenue Act of 1916). Where a return was filed as in this case the taxpayer was required to pay the tax within 105 days from due date of return, to-wit: December 12, 1917.

If the company had failed to make a return of its income for the fiscal period ending June 30, 1917, within sixty days thereafter, it would have subjected itself to the following penalties: (a). A fine not exceeding $10,000.00, (Sec. 14-c, Revenue Act of 1916), (b). fifty per centum of the amount of the tax, to be added thereto by the commissioner, (Sec. 3176 Revised Statutes of the United States, re-enacted in Section 16, Revenue Act of 1916). The fifty per cent penalty was required to "be collected at the same time and in the same manner as part of the tax."

If the company had not paid the tax due under the then existing law upon the income for the fiscal period ending June 30, 1917, within one hundred five days after

the return was due, to-wit, on or before December 12, 1917, it would have subjected itself, after a ten days' notice and demand thereof by the collector, to a penalty of "five per centum on the amount of the tax unpaid and interest at the rate of one per centum per month upon said tax from the time the same becomes due." (Sec. 14-a, Revenue Act of 1916.)

The taxpayer was not relieved of the foregoing requirements by the Revenue Act of October 3, 1917, because in Section 4 of said act, imposing the War Income Tax, it is provided:

> "The tax imposed by this section shall be computed, levied, assessed, collected, and paid upon the same incomes and in the same manner as the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act."

And in Section 212 of said act, imposing the War Excess Profits Tax, it is provided:

> "All provisions of Title I of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, relating to returns and payment of the tax therein imposed, including penalties, are hereby made applicable to the tax imposed by this title."

In conformity with the above requirements and in order to avoid the penalties set forth above, the company on July 25, 1917, filed with the Collector of Internal Revenue at Omaha, Nebraska, its income tax return for the fiscal eleven-months period ended June 30, 1917, duly subscribed and sworn to, upon Form 1031 (Revised Octo-

ber 1916), being the only form then in use by the Bureau of Internal Revenue for that purpose (R. 165).

The return thus filed shows the capital stock of the company to be $2,000,000.00 and the total amount of bonded, and other interest bearing indebtedness, etc., to be $1,009,671.91, and the net income to be $2,371,997.05, making the total income tax under then existing laws, $47,439.94, which was paid when the return was filed.

The return was audited by H. B. Barnett. Upon the face of this return (R. 165) is a rubber stamp in the top of which in large type is the word, "Assessment," under which is stamped the word "Tax," opposite which are the figures, "373,911.54." Next below is the stamped word "Penalty," opposite which there is no amount inserted. Below this is the stamped word "Basis," opposite which is the following: "R A R 6-30-1919." Outside of the stamped form, but immediately opposite the foregoing quotation, are the initials "HB" of H. B. Barnett, the auditor in the Income Tax Unit of the Internal Revenue Department at Washington, who audited the return and Revenue Agent's report (R. 287, 288). Next below is the word "Date" followed by "Jan. 1920." Next below is the stamped word, "Page," followed by "14", and the stamped word "Line," followed by "1". No other assessment stamp appears upon this return. Diagonally across the top are the rubber stamped words "Return audited."

On August 30, 1917, the company filed its excess profits tax return for the same fiscal period, on Form 1095, also being the only form then in use by the Bureau

of Internal Revenue for that purpose. This return was duly subscribed and sworn to (R. 171). Printed in the heading of this form is the following:

> "This supplemental income tax return is to be filed by all corporations * * having an annual net income in excess of $5,000.00 and making income tax returns on a basis of a properly established fiscal year ending with the last day of some month in 1917 other than December 31."

This return showed the total amount of actual capital invested and used in the business to be $2,100,844.05, made up of actual cash paid in of $2,000,000.00; paid in and earned surplus and undivided profits used or employed in the business to be $100,844.05; total net income for fiscal period $2,371,997.05; total profits in excess of exemption for full fiscal year, $2,998,929.53; and after deducting 5/11 of the excess profits for the entire period, showed a total excess profits for the period January 1, 1917, to June 30, 1917, of $1,199,416.11; making the total amount of tax assessable $95,953.29. This amount was paid on August 30, 1917, the day the return was filed. Stamped on the margin with a rubber stamp are the words, "Return audited."

On September 28, 1917, an amended excess profits tax return on Form 1095 was filed with the Collector at Omaha, covering the fiscal period August 1, 1916, to June 30, 1917, duly subscribed and sworn to, (R. 175) showing the total invested capital and total net income to be the same as the first excess profits tax return. Specific exemption was shown at $4,583.33, instead of $5,000.00, and 8% of total invested capital was figured at

$154,061.90, instead of $168,067.52; the change in these two items being due to the fact that they took 11/12 of the specific exemption and of 8% of the total invested capital in the amended excess profits tax return, instead of 12/12 as was done in the first excess profits tax return. This changed all the subsequent figures and showed an additional tax due of $629.33, which amount was paid to the Collector at Omaha, September 29, 1917. This return also had stamped on the margin with a rubber stamp the words "Return audited."

On October 2, 1917, the company addressed and mailed to George L. Loomis, Collector of Internal Revenue at Omaha, the following letter:

> "If a corporation is dissolved during the fiscal year, is there any ruling as to when it should make up its final report, that is, as soon as possible after the dissolution or at the end of its regular fiscal year? (R. 179)."

to which the Collector replied by letter, dated October 3, 1917,

> "when a corporation dissolves it should make a final return and file with the return evidence that the corporation has been dissolved. The final return is due within sixty days from the end of the fiscal year, it may be filed sooner." (R. 183)

On October 3, 1917, the Revenue Act of 1917 was passed.

On October 27, 1917, L. F. Speer, Deputy Commissioner of Internal Revenue, issued a written opinion that a corporation dissolved in June, 1917, is not subject to

the taxes imposed by the Act of October 3, 1917, "for the reason that the Government cannot revive a dead corporation in order to assess taxes which are imposed by laws enacted subsequent to the dissolution of the corporation." (R. 187) This ruling appears to have been later revoked.

On December 18, 1917, a letter was sent by Gorton Roth to George L. Loomis, Collector of Internal Revenue, Omaha, Nebraska, requesting him to send to Roth supplemental blanks for The Updike Grain Company. (R. 193). On January 29, 1918, upon the form furnished by the collector (R. 341), pursuant to the letter of December 18, 1917, being Form 1031 (revised October 1916) containing the same recitals hereinbefore set forth, the company filed its return of net income for the period July 1, 1917, to August 28, 1917, endorsing same as "Final Report." (R. 197). Attached to the return was evidence that the corporation had been dissolved, as suggested by George L. Loomis, in his letter of October 3, 1917 (R. 201), and that the assets had been distributed among the stockholders (R. 201). This return showed no net income, and was also audited by H. B. Barnett. Stamped in the right-hand side of the first page of the return, is the following: "Investigated by agent. No tax due."

In March, 1918, Gorton Roth, former secretary of the company, received through the mail, in an envelope addressed to The Updike Grain Company, without any letter of transmittal, or demand that an additional return be filed (R. 95), blank Form 1031 (revised January,

1918). This form no doubt being sent out by the Collector, in the regular routine of sending forms to all taxpayers annually at that time of year. Thereupon Roth addressed and mailed to the Collector of Internal Revenue at Omaha the letter of March 26, 1918, a communication stating that The Updike Grain Company was dissolved in 1917, and transacted no business after August 27, 1917; that prior to the dissolution of the company, in pursuance of Article 85 of the Income Tax Regulations, as supplemented by the ruling of the Acting Commissioner of March 22, 1917, the corporation retained from its assets, and paid Federal income tax and excess profits tax for the fractional part of the year 1917, "such payments being made in pursuance of the final and fiscal returns duly made and filed in accordance with said rulings;" that prior to dissolution, the company had paid all of its indebtedness in full, and had no indebtedness outstanding or unpaid when dissolved; that all of its assets were distributed to its stockholders at the time of dissolution; that there was not in existence any money or property of the company, nor any officers, directors or stockholders; that he was the former secretary of the company, and was giving the Collector these advices because he was aware of regulation known as Article 61 in reference to the Income Tax Act of October 3, 1917, which, he was advised, is erroneous, and "in order that a statement of the facts in this matter may be made for your records." (R. 91). Although the Collector was thus expressly advised, as aforesaid, no demand was ever made upon the company or its officers by anybody for additional returns (R. 95, 349, 350), notwithstanding Regulation 33, Article 196, effective January

6, 1914, and in force up to December 31, 1921, which was as follows:

> "Where the required returns are not filed within the prescribed time, either by individuals or corporations, notice on Form 1045 should in each case be sent to the delinquent."

During the month of October, 1918, L. C. Smith, Revenue Agent, under the direction of John J. Gillin, Revenue Agent in charge of the Omaha division, and in charge of revenue agents like Smith, examined the books and records of the Updike Grain Company, then in the possession of former secretary Roth, for the years 1913, 1914, 1915, 1916 and 1917, to determine its tax liability for said years and the fiscal period in 1917 ending June 30th, 1917 (R. 95). Mr. Smith had been furnished with Forms 7894, which were summaries of the returns for 1913, 1914, 1915 and 1916, and had instructions to include in his examination the year 1917 (R. 95). The examination was made to check up the returns for the above years, and Mr. Roth furnished him the necessary books to make the audits and everything he asked for. Smith had no summaries or copies of the returns made for 1917, and asked Roth for his copies. Roth had copies and furnished them to Smith (R. 350). Smith testified that upon completing the audit, which he reported in his letter to Gillin, dated October 25th, 1918, (R. 107), he made up the returns referred to in that report, being a Corporation Income Tax Return on Form 1031, (Revised January 1918), and a Corporation Excess Profits Tax Return on Form 1103, (R. 131, 135), and presented them to Nelson B. Updike, the president; and, he believed, to Mr. Roth, the secretary, who said the corpora-

tion had been dissolved and there were no officers with authority to sign the returns, (R. 96). Mr. Roth testified that Mr. Smith never presented those returns to him, and that he never saw them, (R. 349). Mr. Updike testified that Mr. Smith did not present to him any income tax returns for signature, nor did he see any income tax returns prepared by L. C. Smith. (R. 350).

Under date of October 25, 1918, L. C. Smith, Revenue Agent, made a written report to John J. Gillin, Revenue Agent in Charge, Omaha, Nebraska, showing additional taxes due for 1915, 1916 and 1917 and refunds due for 1913 and 1914 (R. 107) The report contains the following recitals:

"With reference to attached Forms 7894 (Revised) showing returns of net income for the years 1913, 1914, 1915 and 1916, filed by the Updike Grain Co., Omaha, Nebr., I have the honor to report that I visited the office of that corporation and *made an investigation of its returns for the years* 1913 *to* 1917, inclusive, returns for prior years having been investigated, and found additional tax liability and refunds due as follows:

	Additional Tax	Refund Due
1913		$258.25
1914		113.01
1915	$ 95.81	
1916	3,094.70	
1917	365,564.61	
Totals	$368,755.12	$371.26

• • • • •

"On account of the inadequate system of accounting kept by this company, it was impossible to make a complete verification of *any return filed, but from all books and records available, it appeared that the full amount of gross income for each year was reported and no improper deductions taken.*

* * * * *

COPY OF RETURN FISCAL YEAR ENDING JUNE 30, 1917

Item 1		$2,000,000.00
2		1,009,671.91
3a	$2,036,898.56	
c	56,252.36	
d	643,791.55	
e	116,657.66	2,853,600.13
4a	375,466.58	
5a	1,277.06	
6a	98,202.35	
7	6,657.09	481,603.08
Net Income		$2,371,997.05
Tax @ 2%		47,439.94

AMENDED RETURN FISCAL YEAR ENDING JUNE 30, 1917

Item 1		$2,000,000.00
2		1,012,771.91
3a	$1,867,157.01	
c	51,564.67	
d	590,142.26	
e	106,936.19	2,615,800.13
4	344,177.70	
5a	1,170.64	
6a	90,018.82	
7	6,102.33	441,469.49
Net Income		$2,174,330.64
Less Dividends (3d)		590,142.26
Income Less Dividends		1,584,188.38

6/11-1917 Proportion		864,102.75
Less Excess Profits Tax		459,081.32
Taxable at 4%		405,021.43
Excess Profits Tax		459,081.32
Income Tax @ 2%		34,304.99
Income Tax @ 4%		16,200.86
Total Tax Liability		509,587.17
Total Tax Paid—		
Income Tax	$ 47,439.94	
Ex. Profits Tax	96,582.62	144,022.56
		$ 365,564.61

2% tax on net income for fiscal period less EPT 1917 portion. Differences:

"*The original return included the business from June* 30, 1916, *to June* 30, 1917, as per book closings of those dates. The end of the fiscal year was redesignated as June 30, and the company given permission to make return on that basis, and the return should have included only eleven months' business from July 31, 1916, to June 30, 1917. It was necessary to adjust the gross income and deductions to that period by eliminating the income and deductions for July 1916, determined by taking 1/12 of the total gross income and deductions of the book closing for the period June 30, 1916, to June 30, 1917.

* * *

"In reply to a letter from the Collector of Internal Revenue for Nebraska, asking for *amended returns* for the year 1917, the enclosed letter (Exhibit A) was directed to his office by Gorton Roth, formerly secretary of the Updike Grain Co.

"*Amended returns* and claims for refund covering adjustments, shown by this report; *for the years,* 1913 to 1917, inclusive, could not be secured, as it was stated by the former secretary of the company

that there were no officers of the company to execute same.

"Unsigned amended returns for the fiscal year (11 months) ending June 30, 1917, are enclosed herewith.

"N. B. Updike, formerly president of the Updike Grain Co. was advised of the differences found and the amount of additional tax resulting therefrom. He stated that it would be necessary to collect the tax from the individual stockholders at the time the company was dissolved, as no provision was made for the payment of this tax before the assets were distributed.

"A list of stockholders on Aug. 28, 1917, the date of dissolution is enclosed herewith." (Exhibit B) (The italics are ours.)

Exhibit "A," referred to in the above report, is the letter of Roth to the Collector dated March 26, 1918.

In the Smith report, noted above, he states that the letter from Gorton Roth, dated March 26th, 1918, to the Collector of Internal Revenue was "in reply to a letter from the Collector of Internal Revenue from Nebraska, asking for amended returns for the year 1917," but Mr. Roth testifies that no such letter was received by him or by the Updike Grain Company, although he handled and saw all of the correspondence had between the Internal Revenue Department and said company with respect to their returns, (R. 95, 349); and Mr. Smith when called as a witness for complainant did not testify that any such letter was sent by the Collector, nor anyone else.

In the same report of L. C. Smith, Revenue Agent, to John J. Gillin, Revenue Agent in Charge, dated October 25, 1918, Mr. Smith says:

"*In addition to verification of income tax returns of the Updike Grain Company,* Omaha, Nebr., I have the honor to report that I made a careful examination of the books and records of the company for the purpose of preparing excess profits tax return on Form 1103, *as required by the Act of October* 3, 1917, and found as follows:

Excess Profits Tax Summary.

Tax Liability under Act of October 3, 1917	$459,081.32
Tax paid under Act of March 3, 1917	96,582.62
Additional Tax Due	$362,498.70"

(The italics are ours). (R. 117).

Then under the heading "Copy Excess Profits Tax Return on Form 1095 under Act of March 3, 1917," he sets forth a synopsis of that return. (R. 117) Then under the heading "Synopsis of Amended Return" he sets forth the return as he concludes it should have been made, and computes the total tax due for the period January 1, 1917, to June 30, 1917, to be $459,081.32. (R. 119) Then appears the following recital:

> "An unsigned *amended return* on Form 1103 is enclosed herewith, as there are no officers of The Updike Grain Company to sign name, the company having been dissolved August 28, 1917." (R. 121) (Italics are ours).

A list of the stockholders of the company and their stockholdings was attached to the report as Exhibit B. (R. 129).

The returns on Forms 1031 (Revised January 1918) and Form 1103, prepared by Smith, contained the sum-

mary of items, as above set forth in his report, and the details making up those items, such as appeared in the returns filed by the grain company. It should be noted at this time that in recalculating the tax for additional assessment under the October 3, 1917 Act, Mr. Smith used the same numbered items that appeared in the returns filed by the grain company for the fiscal period in question, except, of course, he added the additional four percent tax imposed by the Revenue Act of October 3, 1917, and made certain deductions for which the company had made no claim in the returns filed by it, and for which it, of course, was not obliged to make claim. In other words, Mr. Smith's report demonstrates that the company in its returns, as filed, had set forth in good faith all of the items of income, and the facts, data and information appropriate to determine the tax under the new law.

On October 26, 1918, John J. Gillin, Revenue Agent in Charge, addressed and transmitted to Daniel C. Roper, Commissioner of Internal Revenue, the report of L. C. Smith, with four Forms 7894, and the amended returns prepared by Smith on Forms 1031 and 1103, with the letter of Gorton Roth of March 26, 1918, and two balance sheets. The transmittal letter (R. 105) is as follows:

> "I am in receipt of the attached report from Revenue Agent L. C. Smith, dated October 25, 1918, on the subject of his investigation of *the returns of annual net income of the Updike Grain Company,* Omaha, Nebraska, *for the years* 1913 to 1917, inclusive, and also invested capital and income subject to Excess Profits Tax for 1917.

"I respectfully recommend that this corporation be assessed additional tax for 1915, $95.81; for 1916, $3094.70; and for 1917, $365,564.61. Total $368,755.12.

"Forms 7894 for the years 1913 to 1916, inclusive, unsigned Form 1031, unsigned Form 1103, copy of letter dated March 26, 1918, from Gorton Roth to the Collector, and balance sheets as of June 30, 1916, and June 30, 1917, are enclosed herewith.

"Copy of this report, together with Excess Profits Tax Report, furnished Collector Loomis, Omaha, Nebraska." (Italics are ours).

On June 30, 1919, L. C. Smith, Revenue Agent, made a supplemental report to John J. Gillin, Revenue Agent in Charge, correcting the computation of additional tax for the fiscal year ended June 30, 1917, and finding the additional tax to be $373,911.54. (R. 103) Upon the same date Gillin transmitted to the Commissioner of Internal Revenue a copy of this report. (R. 101) On the right hand margin of page 4 of the copy of the Smith report dated October 25, 1918, sent to the Commissioner of Internal Revenue by Gillin and opposite the computation under the heading, *"Amended Return Fiscal Year Ended June* 30, 1917," the tax is recomputed in pencil, and the additional tax due computed to be $373,911.54. (R. 113)

On November 20, 1919, an acting assistant to the Commissioner wrote to the Internal Revenue Agent in Charge, in Omaha, with reference to the report dated October 26, 1918, and the supplemental report dated June 30, 1919, covering the investigation by Revenue Agent L. C. Smith (R. 283) in which it is stated:

"The additional tax still due by the corporation for the eleven months ended June 30, 1917, $373,911.54, is clearly stated in your supplemental report of June 30, 1919. * * * You are instructed to advise the corporation of the result of this audit. A copy of this letter is being forwarded to the Collector for the District of Nebraska."

Also advising as follows:

"Since the corporation failed to file a claim for refund of overpayment for 1913 amounting to $258.25, this office is barred by Section 252 of the Revenue Act of 1917, in offsetting the amount against the additional taxes found to be due."

Thus taking advantage of a statute of limitations against the company.

On November 24, 1919, Gillin, Revenue Agent in Charge, addressed a letter to The Updike Grain Company, (R. 317) as follows:

"This office is in receipt of a letter from the Commissioner of Internal Revenue under date November 20, 1919, relative to investigation of *your income tax returns for the years* 1913 to 1917, inclusive, made by Revenue Agent L. C. Smith, which advises as follows: (The italics are ours).

He then sets forth that part of the letter referred to showing the computations made and the total taxes due and the position that a refund for 1913 is barred. He then concludes the letter as follows:

"The Collector in your district will advise you as to the time and manner of payment of net additional tax."

On November 24, 1919, Gillin, Revenue Agent in Charge, addressed and sent a letter to N. B. Updike (R. 323) as follows:

> "There is enclosed, as requested by your Mr. Roth today, two copies of the following, as shown by the files of this office, in reference to the investigation of the Updike Grain Company:
>
> "*Amended Return,* as made by the investigating officers for the year 1913 and the fiscal years 1914, 1915, 1916 and 1917;
>
> "*Synopsis of Amended Return* for Excess Profits for the fiscal year 1917; and
>
> "*Revised Tax Computation* for the fiscal year 1917, in accordance with Department Letter." (Italics are ours).

The enclosure (R. 325, 335) sets forth the recomputation made by the Revenue Agent respecting the income and excess profits taxes for the year 1917 under the heading, "*Fiscal year ending June* 30, 1917," and under the heading "*Copy of Return*" sets forth a synopsis of the return filed July 25, 1917; and under the heading "*Amended Return*" sets forth the computation as made by Revenue Agent L. C. Smith under dates of October 25, 1918, and June 30, 1919, and at the conclusion of that part of the report made by L. C. Smith dated October 25, 1918, is the following:

> "*The original return* included the business from June 30, 1916, to June 30, 1917, as per book closings of those dates. The end of the fiscal year was redesignated as June 30, and the company given permission to make return on that basis and the *return* should have included only 11 months business from July 31, 1916, to June 30, 1917. It was necessary

> to adjust the gross income and deductions to that period by eliminating the income and deductions for July, 1916, determined by taking 1/12 of the total gross income and deductions of the book closing for the period June 30, 1916, to June 30, 1917." (The italics are ours).

The Revenue Agent in Charge thereby assured the defendants that the returns filed by the company were being recognized and used by the Government as sufficient under the October 3, 1917 Act.

It was apparently on or about the date of the letter of November 20, 1919, from the Acting Assistant Commissioner to the Revenue Agent in Charge, that the assessment in the above amount was stamped upon the income tax return of the company filed July 25, 1917, because the additional tax was placed upon the assessment list by the Commissioner of Internal Revenue for January, 1920. (R. 217, 219, 301).

We do not have a copy of any notice and demand for tax sent out immediately after the assessment of January, 1920, was made, but Mr. Roth testified that a notice and demand was sent to The Updike Grain Company, upon the form in use then, which was either Form 1-17a or 1-17a revised January, 1920. However, both forms contain the following recital:

> "Notice is hereby given that there has been assessed against you the amount of tax stated on this notice. Demand is hereby made for the immediate payment of said tax."

In the notices and demands for the additional taxes assessed in January, 1920, sent out immediately after the assessment, and periodically up to December 22, 1921, there was no claim for any penalties for failure to file a return, and the books of the Collector at Omaha contain no assessment of any penalty for failure to file a return, and none was ever made (R. 148). If a penalty had been assessed, it would appear upon the books of the Collector the same as any other assessment (R. 148).

On April 27, 1923, A. B. Allen, then Collector at Omaha, wrote a letter to the Commissioner of Internal Revenue at Washington, calling attention to the additional assessment against the Updike Grain Company and additional assessments against other dissolved companies in which Mr. Updike was interested (R. 225), stating that he had had the matter up with Mr. Updike a number of times, but did not know how to proceed. He thereupon stated the facts respecting the dissolution of the corporations and the distribution of their assets among their stockholders during the month of August, 1917; that "it is claimed by the taxpayers that they made returns for the part of the year 1917 up to the time of dissolution, and paid the tax as determined up to that time"; that there is no property of the corporations which could be seized by distraint; that Mr. Updike seemed to think there were legal principles involved and a court decision that would constitute a defense, and asked if he might suggest to the taxpayers a reasonable compromise, although he did not know that the taxpayers would entertain the idea of a compromise.

On May 2, 1923, H. F. Mires, Acting Deputy Commissioner, answered the above letter (R. 229) stating that

inasmuch as some of the stockholders have died and there is no property of the corporations which could be seized by distraint, a collection could apparently only be made by suit; he was requesting the Solicitor of Internal Revenue to prepare an opinion on the matter.

On May 8, 1923, Collector Allen wrote to Mr. Updike (R. 343) advising him that the matter of the additional taxes of the dissolved corporation had been referred to the Solicitor of Internal Revenue for an opinion as to the liability of the stockholders.

On May 8, 1923, C. R. Nash, Deputy Commissioner, sent to the Collector at Omaha a copy of the opinion of the Solicitor of Internal Revenue, referred to above (R. 233), wherein it was stated:

> "It appears that all of these corporations were dissolved and the assets distributed among stockholders during the summer of 1917 and prior to the passage of the Revenue Act of 1917. The latter states that the corporations made returns for a fractional part of the year 1917 up to the time of distribution and paid the tax under the rates in force at that time. A later audit of the returns resulted in additional assessments due to the provisions of the Revenue Act of 1917, which were retroactive in application. Assuming that returns were filed in August, 1917, suit for the recovery of additional taxes for the year 1917 was barred in August, 1922, under the provisions of Section 250 (d) of the Revenue Act of 1921. As the corporations have been dissolved, warrant of distraint against the corporations cannot be enforced as against stockholders of the former corporations and unless the stockholders voluntarily submit an offer in compromise of the amount of the tax there is no means of enforcing liability.

> If the corporations have any property distraint will lie providing the assessment was made within the period of limitation as prescribed by Section 250 (d) of the Revenue Act of 1921."

Collector Allen immediately upon being advised that the right to collect taxes was barred, and that there was no means of enforcing the liability of the stockholders, conferred with Mr. Updike, but did not inform him of the opinion of the Solicitor of Internal Revenue that the tax was barred, and finally induced him to make an offer of settlement in the amount of $10,000, which the Collector stated was satisfactory, and that he would recommend same for acceptance by the Department. Thereupon he induced Mr. Updike to give him a check for $10,000, which he promised not to cash until the offer was accepted. The check, however, was cashed by the Collector shortly thereafter (R. 350, 351).

On June 5, 1923, the Collector wrote to the Commissioner (R. 279) transmitting the offer of compromise, and stating

> "due to the fact that suit for recovery for additional taxes is barred by the statute of limitations, I am recommending that this offer be accepted. This offer is being taken up in the regular way and will appear on my supplemental June 1923 list, account 540039."

When Updike discovered that the check had been cashed he made repeated requests of Allen for written evidence of settlement. Allen assured him that the claims were settled and that it would simply be a matter of routine to secure evidence of settlement (R. 351).

After other correspondence between the Collector and the Commissioner, Mr. Updike received a letter from the Commissioner dated February 12, 1924, stating that the offer had been rejected (R. 347).

On April 12, 1924, the Government instituted suit against Mr. Updike and other stockholders of the Missouri Valley Elevator Company to recover additional taxes assessed against that company under the October 3, 1917, Act, which company had likewise been dissolved in August, 1917, and was one of the companies included and referred to in all of the correspondence hereinbefore set forth. Returns had been filed for that company in the same manner as they had been filed for the Updike Grain Company (R. 349, 350). In that suit no claim was made that the Missouri Valley Elevator Company had failed to file "a required return" or "a return," but after alleging the facts, respecting the returns actually filed, the complainant charged "said returns were incorrect, misleading and false in law in the respects hereinafter set forth. (R. 355-367).

The Bureau of Internal Revenue, having knowledge of the facts respecting the returns of that company as hereinbefore recited, apparently was unwilling to base its delayed right to collect those taxes upon the ground that no return had been filed, but deliberately took the position, in the above Bill of Complaint, that a return had been filed, but that same was "false in law," in order to avoid the limitation provisions in Sec. 250 (d) of the Revenue Act of 1921.

Mr. Updike and the other defendants interested herein were again led to believe by this Bill of Complaint

that the Government was accepting the returns filed as the "required" returns for assessment of the tax imposed by the October 3, 1917 Act, but was only claiming that the returns were false in law because they did not have calculated thereon the correct amount of the tax as imposed by the October 3, 1917 Act. No claim had been made up to that time by any governmental official to any of these defendants that the Updike Grain Company, the Missouri Valley Elevator Company, or any of the other companies in which Mr. Updike was interested, which had been dissolved in the summer of 1917, came within the "no return" class, and no such claim was thereafter made until upon the actual trial of the Missouri Valley Elevator Company case in June, 1924, (R. 350 and 351) after that case had been prepared by the defendants upon the theory that the government was admitting that required returns had been filed, but was only asserting that same were false in law.

It never has been, and can not be, claimed by the Government that the returns filed for any of the companies were false or fraudulent or that any of the defendants were guilty of any fraud, actual or constructive, in any of the matters in controversy herein.

It has been intimated, but without any proof offered or capable of being produced, that the various companies in which Mr. Updike was interested were dissolved to evade taxes under the October 3, 1917 Act. This is not true, except to this extent, that the dissolutions were partly influenced by the unfair provisions of the Revenue Laws, existing at that time, compelling corporations

holding stock in other corporations to pay income taxes upon the dividends from such stock, which provisions were subsequently changed by Congress, because of the injustice of the same.

From all the facts and circumstances the conclusion is irresistible that the Commissioner accepted the returns made by the company covering the fiscal period ending June 30, 1917, which were filed in July, August and September, 1917, for the following among other reasons:

(a) The returns as filed by the Updike Grain Company set forth specifically the gross amount of income from all separate sources of said company for the year 1917 and for the eleven month period ending June 30th, 1917, and the aggregate items of allowance claimed by the company and authorized by law, and the total and entire net income and earnings of the company for such eleven month period and for the periods January 1, 1917 to June 30, 1917 and July 1, 1917, to the date of dissolution of the company in August, 1917, and all other facts, data and information appropriate and necessary to determine the net income and to carry out any applicable provisions of the Revenue Act of October 3, 1917.

(b) No notice, demanding additional returns, was sent to the company as required by Regulation 33, Article 196, supra.

(c) When the Commissioner requested the Revenue Agent in Charge at Omaha to make an audit of the books and records of the company to ascertain the amount of additional tax due, he requested him to audit the 1917 returns of the company which had been filed, and did not claim or advise that no return had been filed.

(d) The Revenue Agent making the audit for the year 1917 asked for, received and used the copies of the returns filed by the company for that year in making his examination and audit.

(e) The Revenue Agent in Charge and the Revenue Agent making the examination proceeded upon the theory that a return had been made, which their correspondence clearly indicates.

(f) In the report of the Revenue Agent making the examination, he refers to the computations for the year in question as an "*amended return,*" which designation was apparently accepted by the Commissioner, because it was upon the figures thus set forth that the Commissioner determined and assessed the tax.

(g) The Revenue Agent, making the examination and audit of the 1917 returns, prepared "a return" for the Commissioner pursuant to Sec. 14 (a), Revenue Act of 1916, both for the War Income and Excess Profits Tax under the October 3, 1917 Act.

(h) No penalty was assessed against the company for failure to file a return, which it was the duty of the Commissioner under the regulations and law to assess where no return had been filed, and had he not been accepting the returns filed as sufficient. (Sec. 1004, Rev. Act, 1917; Reg. 33, Art. 21; Reg. 33, Art. 197; Reg. 33, (Rev.) Art. 214, para. 629).

(i) In a letter dated April 27, 1923, from the Collector of Internal Revenue, Omaha, Nebraska, to the Commissioner of Internal Revenue, attention is called to this tax, and in that letter it is stated:

> "It is claimed by the taxpayers that they made returns for the part of the year 1917 up to the time of the dissolution."

(j) The Solicitor of Internal Revenue in his opinion of May 4th, 1923, recognized the fact that returns had been filed for the period in question.

(k) The Bureau of Internal Revenue and the Department of Justice, in the suit brought against Mr. Updike to recover the taxes assessed against the Missouri Valley Elevator Company, recognized that the returns filed by that company, which were of like character to the returns filed for the Updike Grain Company, were sufficient returns to start the running of the statute of limitations in cases where returns had been filed, had they not charged them to be "incorrect, misleading and false in law."

It appears from the foregoing that the returns filed by the company were recognized as sufficient under the October, 1917, Act, (1) by the Collector of Internal Revenue at Omaha; (2) by the Commissioner of Internal Revenue, in directing a revenue agent to make the investigation, who was empowered to do so only in cases where returns were made; (Reg. 33, Art. 186; Treas. Dec. 1932, para. 5; Reg. 33 (Rev.) Art. 221, para. 639; Reg. 45, Art. 1012) (3) by the Revenue Agent in Charge at Omaha; (4) by the Revenue Agent making the investigation and audit; (5) by the Solicitor for the Bureau of Internal Revenue; (6) by the Proving and Audit Divisions in endorsing the additional assessment on the return; and (7) by the Commissioner of Internal Revenue in making the assessment, as so endorsed; and (8) by the Department of Justice in the Missouri Valley Elevator Company case.

As a result of the foregoing the taxpayer, and likewise the former officers and stockholders, had the right to assume, and at all times did assume, that the returns as filed were sufficient. By the conduct of the various governmental officers recited above, the taxpayer and

the stockholders and transferees were lured and lulled into the belief and security that the company had complied with all the rules, regulations and laws respecting returns, for its income for the year 1917, and had thereby escaped any penalties or disadvantages imposed upon one not filing returns.

Argument Respecting Filing of Returns.

In the Missouri Valley Elevator Company case, in the absence of the proof put in evidence in this case, it was determined that there was no limitation upon the right of assessment and/or collection of the tax in that case because that company had not filed a "required return," and consequently said case came within the following provisions of Section 250 (d) of the Revenue Act of 1921:

> "That in the case of a false or fraudulent return with intent to evade tax, or of a failure to file *a required return,* the amount of tax due may be determined, assessed, and collected, and a suit or proceeding for the collection of such amount may be begun, at any time after it becomes due."

Those provisions were carried into the Revenue Acts of 1924 and 1926, but with a very significant change. They appear in Section 278 (a) of both Acts in the following language:

> "In the case of a false or fraudulent return with intent to evade tax or of a failure to file *a return* the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

You will note the use of the phrase, "a return," in the 1924 and 1926 Acts, as distinguished from the phrase, "a required return," used in the 1921 Act. The limitation provisions in the 1924 and 1926 Acts supersede the limitation provisions in the 1921 Act, and therefore being the law at the time of the commencement of this action, the case must be decided in the light of the provisions of these later Acts.

The effect of this change in the phraseology came before the Board of Tax Appeals in the case of *Werbelovsky, Executor v. Commissioner,* 8 B. T. A. 442, acquiesced in by the Commissioner, Cum. Bull. VII-1, 33. This case involved taxes upon income from the estate of J. H. Werbelovsky for the calendar year 1917.

The executor, on April 1, 1918, filed a fiduciaries' income tax return, on Form 1041, for income for the calendar year 1917, showing no net income. The regulations promulgated by the Commissioner and approved by the Secretary of the Treasury, in force and effect at the time, permitted returns of such fiduciaries to be filed on Form 1041, if the income of the estate was less than $1,000, but further required that if the income of the estate was $1,000 or over, return should be filed on either Form 1041 or 1040-A. The Commissioner, upon later audit and review, found and determined the net income of the estate for the calendar year 1917 to be $192,570.71, and mailed the executor a deficiency letter, in which he notified him of a deficiency against the estate for the year 1917, of $46,419.74. The executor appealed to the Board of Tax Appeals and contended that the proposed de-

ficiency was barred by Section 275 (a) (2) of the Revenue Act of 1924, because the proceedings had been begun against him more than five years after "returns" had been filed. The Commissioner contended that in accordance with the Revenue Act of 1916, he was given authority, subject to the approval of the Secretary of the Treasury, to prescribe the form or forms to be used by all taxpayers in reporting their income; that pursuant to such authority, he with the approval of the Secretary, promulgated certain regulations providing that in all cases of reporting under section 2 (b) of the Revenue Act of 1916, as amended, a return should be filed on Form 1040 or 1040-A when the income of the estate, as an entity, was $1,000 or over; that no return had been filed on either Form 1040 or 1040-A; and that, therefore, in accordance with section 278 (a) of the Revenue Act of 1924 the tax in question could be assessed or a proceeding in court for its collection could be begun without assessment at any time. The Board of Tax Appeals held as follows:

> "We are of the opinion that both the assessment and collection of the tax here in question are barred by the statute of limitations. * * *
>
> "* * * Does the fact that the executor who filed the return for the estate did not include in such return certain income which the Commissioner has determined was income of the estate, but which the estate still denies was income, or the fact that the executor in filing 'a return of the income' used form 1041 instead of either 1040 or 1040-A place the estate in the position of having failed to file a return

within the meaning of the words 'or of a failure to file a return' as used in section 278 (a) of the Revenue Act of 1924? We think not. The estate did file a 'return.' The Commissioner has not alleged or contended that the return as filed was either a 'false or fraudulent return with intent to evade tax.' Under such facts and circumstances we fail to find any authority in section 278 (a) for the proposition that the taxes here in question could be assessed or a proceeding in court for their collection could be begun without assessment at any time.

"The respondent in effect is asking us to read into section 278 (a) the word 'required' as if the statute read 'or of a failure to file a required return.' This we cannot do. The word 'required' was in a similar provision of the Revenue Act immediately prior to the Revenue Act of 1924. See the second proviso of section 250 (d) of the Revenue Act of 1921, which reads:

"Provided further, that in the case of a false or fraudulent return with intent to evade tax, or of a failure to file a required return, the amount of tax due may be determined, assessed, and collected, and a suit or proceeding for the collection of such amount may be begun, at any time after it becomes due.

"It must be assumed that Congress intended to omit the word 'required' in the latter act.

* * * *

"The Commissioner was put on notice that a return had been filed and was given five years to examine the return and determine whether any taxes were due. This he did not do until after more than two and one-half years after the five-year period had expired. We are, therefore, of the opinion that the assessment and collection of the taxes now proposed by the respondent are barred by the statute of limitations. Compare *Appeal of Mabel Elevator Co.*, 2 B. T. A. 517, and *Bastrop Mercantile Co., Let., v. Commissioner*, 7 B. T. A. 529."

In *Brewster v. Gage*, Dec. 6th, 1929, this court held:

> "The deliberate selection in a statute of language differing from that of earlier acts on the subject indicates that a change of law was intended."

The change in the phraseology was undoubtedly prompted by the settled policy of Congress,—as demonstrated by the various Revenue Acts enacted during the past ten years,—to extend the limitation provisions, respecting assessment and/or collection of income, excess-profits, and war-profits taxes, to all cases wherein the Government had obtained knowledge of an income through any return filed, whether or not same was upon any particular form of return, contained the correct gross or net income, contained a correct calculation of the tax, or failed to comply with other details respecting the law or regulations where the taxpayer was not guilty of any fraud. The courts and the Board of Tax Appeals have recognized and carried out that policy in their decisions, as will be hereinafter shown.

It must be conceded that if "a return" was filed either (a) by the taxpayer or (b) by the Commissioner of Internal Revenue, more than five years before this action was brought, the right to collect the tax is barred by Section 250 (d) of the Revenue Act of 1921, Section 277 (a) (2) of the Revenue Act of 1924 and Section 277 (a) (3) of the Revenue Act of 1926.

(a)

Was "A Return" Made and Filed by the Taxpayer?

The relevant provisions of the Revenue Acts of 1916 and 1917 are as follows:

Section 13 (b) of the Revenue Act of 1916 (39 Stat. 771):

> "Every corporation, joint-stock company or association, or insurance company, subject to the tax herein imposed, shall, on or before the first day of March, nineteen hundred and seventeen, and the first day of March in each year thereafter, or, if it has designated a fiscal year for the computation of its tax, then within sixty days after the close of such fiscal year ending prior to December thirty-first, nineteen hundred and sixteen, and the close of each such fiscal year thereafter, render a true and accurate return of its annual net income in the manner and form to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and containing such facts, data, and information as are appropriate and in the opinion of the commissioner necessary to determine the correctness of the net income returned and to carry out the provisions of this title. The return shall be sworn to by the president, vice president, or other principal officer, and by the treasurer or assistant treasurer. The return shall be made to the collector of the district in which is located the principal office of the corporation, company, or association, where are kept its books of account and other data from which the return is prepared, * * * All such returns shall as received be transmitted forthwith by the collector to the Commissioner of Internal Revenue."

Section 3173 of the Revised Statutes of the United States, as amended by Section 16 of the Revenue Act of 1916 (39 Stat. 774):

the sudden enactment in close proximity to each other of the Revenue Acts passed September 8th, 1916, March 3d, 1917 and October 3d, 1917, imposing additional income, war income and war excess profits taxes, with their many varied and complicated provisions and department regulations, new to income tax laws. Even if this regulation were specific and unambiguous, the same does not have the force of a statute or even of a judicial determination as will be seen by the opinion in *Stieff vs. Tait*, 26 Fed. (2d) 489, (D. C. D. Md.), wherein it is held, as announced in the syllabus, as follows:

> "Regulations of the Commissioner of Internal Revenue, constituting merely interpretation of law by an administrative office, are of no more than persuasive authority and do not have the force of judicial determination."

Whether that regulation was ambiguous or not, the discretionary powers of the Commissioner gave him authority to interpret and even waive the requirements of that regulation as subsequently interpreted in the Missouri Valley Elevator Company case. Neither the Commissioner nor the Collector of Internal Revenue demanded new or additional return of the 1917 income. The revenue agent who audited the books prepared what he termed an "amended" return, which he states was not signed because there were no officers of the dissolved company at the time. But at no time did anyone assert that it was necessary for the taxpayer to go through the useless formality of filing another return, which would set forth no information additional to that contained in the returns already on file. We can only conclude from all the facts and circumstances in this case that the Commis-

sioner accepted and adopted the returns filed by the taxpayer as sufficient and effective for assessment of the additional tax specified in the October 3rd, 1917 Act. All of the officials having anything to do with the determination or calculation of the additional tax, designated the returns filed by the taxpayer as returns for the additional tax under the October 3rd, 1917 Act, and referred to the returns made up by the Revenue Agent in his report and upon the separate forms as "amended" returns and not as initial returns. Having indicated to the taxpayer and the former officers of the taxpayer that the returns filed by the taxpayers were being accepted and adopted by the Bureau of Internal Revenue as sufficient under the October 3d, 1917, Act, common honesty and justice require that the Government be estopped from endeavoring to place the taxpayer or the defendants in this case in the unfavorable position of the taxpayer who failed to file "a return."

Where estoppel depends upon the conduct of an officer having such wide discretionary powers as the Commissioner of Internal Revenue with respect to the matters involved, it applies to the Government in such cases the same as to any other litigant. In the case of *Dayton Airplane Co. v. United States*, 21 Fed. (2d) 673, (6th C. C. A.), it is said:

> "It is first to be observed that this contract and the actions under it were not made or taken by officers who must find in a statute clear authority for their every act. In such contracts with such an officer the public is dealing with an agent of known and limited powers. Once beyond these powers, principles of estoppel or fair dealing have no application against

"It shall be the duty of any person, partnership, firm, association, or corporation, made liable to any duty, special tax, or other tax imposed by law, when not otherwise provided for, (1) in case of a special tax, on or before the thirty-first day of July in each year, (2) in case of income tax on or before the first day of March in each year, or on or before the last day of the sixty-day period next following the closing date of the fiscal year for which it makes a return of its income, and (3) in other cases before the day on which the taxes accrue, to make a list or return, verified by oath, to the collector or a deputy collector of the district where located, of the articles or objects, including the amount of annual income charged with a duty or tax, the quantity of goods, wares, and merchandise, made or sold and charged with a tax, the several rates and aggregate amount, according to the forms and regulations to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, for which such person, partnership, firm, association, or corporation is liable. * * *"

Section 19, Revenue Act of 1916:

" * * * If the collector or deputy collector have reason to believe that the amount of any income returned is understated, he shall give due notice to the person making the return to show cause why the amount of the return should not be increased, and upon proof of the amount understated may increase the same accordingly. * * * "

Section 4, Revenue Act of 1917 (40 Stat. 302):

"That in addition to the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, there shall be levied, assessed, collected, and paid a like tax of four per centum upon the income received in the calendar year nineteen hundred

and seventeen and every calendar year thereafter, by every corporation, joint-stock company or association, or insurance company, subject to the tax imposed by that subdivision of that section, except that if it has fixed its own fiscal year, the tax imposed by this section for the fiscal year ending during the calendar year nineteen hundred and seventeen shall be levied, assessed, collected, and paid only on that proportion of its income for such fiscal year which the period between January first, nineteen hundred and seventeen, and the end of such fiscal year bears to the whole of such fiscal year.

"The tax imposed by this section shall be computed, levied, assessed, collected, and paid upon the same incomes and in the same manner as the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, except that for the purpose of the tax imposed by this section the income embraced in a return of a corporation, joint-stock company or association, or insurance company, shall be credited with the amount received as dividends upon the stock or from the net earnings of any other corporation, joint-stock company or association, or insurance company, which is taxable upon its net income as provided in this title."

Section 200, Revenue Act of 1917 (40 Stat. 302):

" * * * If a corporation or partnership, prior to March first, nineteen hundred and eighteen, makes a return covering its own fiscal year, and includes therein the income received during that part of the fiscal year falling within the calendar year nineteen hundred and sixteen, the tax for such taxable year shall be that proportion of the tax computed upon the net income during such full fiscal year which the time from January first, nineteen hundred and seventeen, to the end of such fiscal year bears to the full fiscal year; * * *"

Section 1004, Revenue Act of 1917 (40 Stat. 325):

"That whoever fails to make any return required by this Act or the regulations made under authority thereof within the time prescribed or who makes any false or fraudulent return, and whoever evades or attempts to evade any tax imposed by this Act or fails to collect or truly to account for and pay over any such tax, shall be subject to a penalty of not more than $1,000, or to imprisonment for not more than one year, or both, at the discretion of the court, and in addition thereto a penalty of double the tax evaded, or not collected, or accounted for and paid over, to be assessed and collected in the same manner as taxes are assessed and collected, in any case in which the punishment is not otherwise specifically provided."

Section 1005, Revenue Act of 1917 (40 Stat. 326):

"That the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, is hereby authorized to make all needful rules and regulations for the enforcement of the provisions of this Act."

As heretofore shown, the taxpayer filed returns of its gross and net income for the fiscal period ending June 30th, 1917, which contained "such facts, data, and information" as were "appropriate" and "necessary to determine the correctness of the net income return." This was so determined by the revenue agent representing the Commissioner of Internal Revenue who audited the return. In the report of his audit, dated October 25th, 1918, he said:

"I visited the office of that corporation and made an investigation of its returns for the years 1913 to 1917 inclusive. * * * From all books and records avail-

able, it appeared that the full amount of gross income for each year was reported and no improper deductions taken."

It appears from the provisions of the Revenue Acts of 1916 and 1917 quoted above, that the Commissioner was given wide discretion respecting the form, contents and acceptance or rejection of returns made under both the 1916 and 1917 Acts, and in making and enforcing regulations respecting same. He was also possessed of wide powers under the general law. In Revised Statutes, Section 321, Chapter 223, found in Section 2, Chapter 1, Title 26 United States Code, his duties were defined as follows:

> "The Commissioner of Internal Revenue, under the direction of the Secretary of the Treasury, shall have general superintendence of the assessment and collection of all duties and taxes imposed by any law providing internal revenue; and shall prepare and distribute all the instructions, regulations, directions, forms, blanks, stamps, and other matters pertaining to the assessment and collection of internal revenue; * * "

The Commissioner could accept any kind of a list or statement the taxpayer may file as the return of the taxpayer. When he did so it then constituted the return of the taxpayer.

The record shows that in this case the Commissioner did accept the returns made by the taxpayer in July, August, and September, 1917, as its returns for assessment of the tax under the October 3d, 1917, law.

Although Regulation 33 (Revised), Article 61, was promulgated in January, 1918, it received no interpretation with respect to corporations, dissolved in 1917, having previously filed returns of their 1917 incomes, until the Missouri Valley case was determined.

Article 61 referred to above is as follows:

> "A corporation which was dissolved in 1917, prior to passage of war revenue Act of October 3, 1917, is subject to tax under the Act of September 8, 1916, as amended, and also to the war income tax and the war excess profits tax imposed by the Act of October 3, 1917. (*Brady, et al. v. Anderson*, 240 Fed. 665). Corporations so situated will make a return on revised Form 1031, covering the period in 1917 during which it was in business prior to its dissolution. If it shall have previously made a return covering this period and shall have paid any excess profits tax under the Act of March 5, 1917, it shall be entitled to credit for the amount of such tax so paid against any excess profits tax assessable against it under Title II of the Act of October 3, 1917."

It is claimed that notwithstanding the law and regulations, existing at the end of the fiscal period June 30, 1917, required the company to file returns within sixty days thereafter, and imposed sever[illegible] penalties for any failure in that respect, this regulation imposed upon the company the duty of filing an additio[illegible]al return for the fiscal period ending June 30, 1917.

We are of the firm belief that such inte[illegible]retation is not justified by a reasonable and fair construc[illegible] of the regulation in the light of the facts and circumsta[illegible]es surrounding the situation. We appreciate the fact that this regulation was so interpreted in the Missouri Valley Ele-

vator Company case, but on account of the confusion over the issues in that case, we feel that the interpretation of that regulation did not receive the attention in that case that it might otherwise have had. We, therefore ask for a decision of this question by this court, and in doing so keep in mind the effective date of the regulation and the distinction between corporations dissolved in 1917, operating upon a calendar year basis, and those operating upon a fiscal year basis. The regulation was not promulgated until January 2nd, 1918, which date was more than four months after corporations operating upon a fiscal year basis ending June 30, 1917, had, and were required to file their returns, but in ample time to govern the returns of corporations dissolved in 1917, operating upon a calendar year basis, as their returns would not be due until March 1st, 1918. We must also bear in mind that the Act of October 3, 1917, merely increased the percentage of tax upon the subjects or items specified in the Revenue Act of 1916, consequently the Government would require no additional data upon which to calculate the tax than would be, and was in the instant case, set forth in returns upon the forms used under the 1916 Act.

An additional return, therefore, would give the Government no additional information necessary for calculation of the tax and would be imposing upon the taxpayer a useless and meaningless burden, for the neglect of which he would be subjected to the severe penalties attaching to a failure to file a return.

In analyzing this regulation in the light of the foregoing it will be noted that Article 61 does not specifically

distinguish between corporations operating under a calendar year basis and those operating upon a fiscal year basis, but by applying the rule of reasonable construction it is apparent that a second sentence was intended for corporations operating upon a calendar year basis only and the third sentence for those operating upon a fiscal year basis. A fair construction therefor is that corporations dissolved in 1917 which were operating upon a fiscal basis and which had previously made a return, were not required to file another return, as the returns made must necessarily set forth the data upon which the additional tax could be calculated. This regulation having become effective January 2, 1918, that part thereof requiring a return upon revised Form 1031 (revised January 1918), could well apply to corporations operating upon a calendar year basis, as their returns were not due until March 1, 1918. In the absence of a specific provision clearly imposing upon those corporations "having previously made a return" upon a fiscal year basis, the duty of filing a second return, it would seem that if the Commissioner intended that those corporations should make additional returns and suffer any penalties or loss of rights in the event of failure, it would have and should have been specifically so stated.

It should also be noted that the requirement in this article is to "make a return on Revised Form 1031." The form used by the company in making its return "covering the period in 1917 during which it was in business prior to its dissolution" was "Revised Form 1031," (See Ex. 7, p. 165 and Ex. 14, p. 197). It is true that the Revised Form 1031 used by the company in making its

return was Form 1031, (Revised October 1916) but the above article did not specifically state which revised issue of Form 1031 was required. It would seem reasonable and just that if the government was going to claim any advantage from a regulation that a failure to comply with might result in severe penalties upon the taxpayer, it should make that regulation more specific.

Before leaving this subject, we should direct attention to the fact that the regulations of the Bureau of Internal Revenue in both 1917 and 1918 required corporations to file two returns for each tax period, one designated as an "Income Tax Return" which was Form 1031, and the other designated as an "Excess Profits Tax Return" which, for the year 1917, was on Form 1095, and for returns made in 1918 was upon Form 1103. It will be noted that Article 61, Regulation 33 (Revised) did not require any additional Excess Profits Tax Returns, consequently it must have been intended to accept any excess profits tax return, that had been filed by a dissolved corporation in 1917, as sufficient under the October 3, 1917 Law, as there was no regulation requiring the taxpayer to file an additional excess profits tax return upon Form 1095, Form 1103, or upon any other form. The Excess Profits Tax Return, Form 1095, already filed, was thereby declared to be sufficient, and as this represented $362,498.70 of the total alleged deficiency, the alleged deficiency to that extent, at least, is clearly barred.

In considering the good faith of the taxpayer and respondents, we should remember that much confusion necessarily resulted among all taxpayers, as a result of

his principal. Here the scope of the contract is not limited by any statute. The government was acting by the Secretary of War, in a national emergency of the first class. His discretion was unlimited; it must be exercised through subordinates; in the absence of fraud or bad faith, the exercise of such delegated authority is the Secretary's exercise of it. Rules of estoppel and fair dealing apply in full force as with individuals. In this class of contracts, and for effect on future emergencies, if for no other reason, a sound public policy must require that the government keep its contracts and stand by its settlements as an individual must. In that atmosphere the questions of this case are to be approached."

See also *The Falcon*, 19 Fed. (2d) 1009.

That the Commissioner's acceptance of a return need not be formal but may be shown by conduct, is sustained by General Counsel's Memoranda No. 1682-VI-22-3250, in an analogous matter, wherein the Commissioner was insisting upon the validity of a waiver unsigned by the Commissioner extending the time for collection of a tax that otherwise would have been barred by the Revenue Act of 1924. Section 278 (e) of the Revenue Act of 1926 provides that Section 278 shall not authorize the assessment of a tax or the collection thereof, if at the time of the enactment of the 1926 Act such assessment or collection was barred, "unless prior to the enactment of this Act the Commissioner and the taxpayer agreed in writing thereto." The waiver relied upon by the Commissioner was signed by the taxpayer, but was not signed by the Commissioner, and the taxpayer challenged the effectiveness of same for that reason. The General Counsel, in passing upon that question, said:

"This office is therefore of the opinion that the validity of a waiver or agreement by a taxpayer that the statute of limitations with respect to collections shall be waived, which was executed by the taxpayer prior to the enactment of the Revenue Act of 1926, is not affected by the absence of the Commissioner's signature where the Commissioner has otherwise indicated his acceptance of the taxpayer's offer to waive the statute of limitations by reliance on, or parol acceptance of, the waiver in its terms."

Returns, to start the running of the statutes of limitations, in the various tax laws, do not have to be letter perfect. A taxpayer, making a good faith return upon a fiscal year basis ending July 31st, 1918, when it should have made its return upon a calendar year basis, cannot be assessed five years after such return was made, on the ground that no return was made, although the return filed was not in strict compliance with the law, and the Commissioner had *demanded* a return on a calendar year basis, which the taxpayer had neglected to file.

United States v. Mabel Elevator Co., 17 Fed. (2d) 109; (D. C. Minn.)

Bastrop v. Commissioner, 7 B. T. A. 529, acquiesced in by Commissioner, Cum. Bull. VII, 1, p. 3.

The filing of an amended return does not interrupt the running of the statute of limitations, but same is held to start running from the filing of the original return, although there may have been a wide discrepancy between the two returns, if there was no fraud.

Franklin v. Commissioner, 7 B. T. A. 636, Acquiesced in by Commissioner, Cum. Bull. VII, 1, p. 11.

Shanley v. Commissioner, 7 B. T. A. 521.
Lancaster Lens Co. v. Commissioner, 10 B. T. A. 1153.

Appeal of National Refining Co., 1 B. T. A. 236.
Lawrence v. Ham, 19 Fed. (2d) 643 (D. C. Me. S. D.)

An unsigned work sheet on Form 1040-A prepared by employes in the office of the Collector of Internal Revenue for a person who could neither read nor write any English, except his signature, but which was accepted by the collector, and a tax assessed thereon has been held to be a return for the year 1919.

Belowsky v. Commissioner, 7 B. T. A. 424.

A corporate return for a fiscal year ending June 30, 1919, which was signed by the Vice President and Secretary, instead of by the Vice President and Treasurer or Assistant-Treasurer, as the law and regulations then required, was held to be in substantial compliance with the statute and to constitute the return "required" by law, and in discussing this question the Board of Tax Appeals said:

> "So far as disclosed, the respondent never at any time prior to the hearing of this appeal made objection to the form or manner in which said document was executed, nor ever at any time requested the petitioner to file a return verified by the affidavit of its treasurer or assistant treasurer.
>
> * * *
>
> "The statute provides that every corporation subject to taxation shall make a return, stating specifically the items of its gross income and the allowable deductions and credits, and further provides that the return shall be sworn to by the president,

vice president, or other principal officer and by the treasurer or assistant treasurer.

"What is the essence of the thing required to be done by this statute? It is, we think, the making of an honest return by the corporation, wherein are set forth specifically the items of its gross income and the allowable deductions and credits, in order that the Commissioner may determine the correct amount of its tax liability. If such required information is fairly and honestly given in a return sworn to by officers of the corporation who are familiar with its affairs, this in our opinion constitutes a substantial compliance with the provisions of the statute.

"The prime object of the legislative intention was manifestly to require that the specified information be furnished under oath by the corporate officers, and where such information is fairly and honestly given in a return sworn to by the vice president and secretary of the corporation the legislative purpose is achieved in no less degree than if the return had been sworn to by the vice president and treasurer or assistant treasurer.

"A general rule of statutory construction is that those provisions which do not relate to the essence of the thing to be done, and as to which compliance is a matter of convenience rather than substance, are directory; while those provisions which relate to the essence of the thing to be done, that is, to matters of substance, are mandatory. 25 R. C. L. 767.

"In Mabel Elevator Co., 2 B. T. A., 517, we said:

"There can be no doubt that such limitations are placed on assessments for the purpose of assuring the taxpayer, who has made an honest return, that after such period his tax liability will not be reopened; otherwise the business of the country would always have before it the threat of additional taxes against the income of years long past whenever a

new theory for interpreting the tax law or for the application of accounting principles occurred to the taxing authorities. If the limitation can be avoided on the plea that the return filed was not such a return as is required by law, although filed in good faith, there is no such assurance for the taxpayer and the limitation becomes of doubtful value at least. If the statute requires any interpretation great weight must be given to the purpose which it was obviously intended to accomplish.

"Again, in Colmer-Green Lumber Co., 12 B. T. A. 256, we said:

> 'The period of limitation prescribed by the statute is one of repose and it should not lightly be construed to permit the respondent to reopen cases upon the ground that the return filed in good faith was not the return required by the statute.'

"In F. A. Hall Co., 3 B. T. A. 1172, a consolidated return was filed for the taxpayer and an associated company, sworn to by the individual who was the treasurer of both companies. The Commissioner contended that separate returns should have been filed, and that the consolidated return filed was not the return required by law; hence, the statute of limitations did not apply. Since it appeared that the consolidated return specifically stated the items of gross income and the items of deductions of the taxpayer, we held that it constituted a substantial compliance with the provisions of section 239 of the 1918 Act, *Supra,* respecting the making of returns, and was sufficient to start the running of the statute of limitations embodied in section 277 (a) (2) of the 1924 Act, *supra.*

"Under the theory contended for by the respondent in this case, if a corporation had no treasurer or assistant treasurer, or if such office was vacant through resignation, death or otherwise at the

time of making its tax return, such facts would operate to place the corporation beyond the purview of the statute of limitations, and would deny to it the right of any benefit thereunder. We are not persuaded that this was the intention of Congress.

"The good faith of the petitioner in making the return involved herein is not questioned by the respondent, and said return specifically stated the items of its gross income and the allowable deductions and credits. It is our opinion, therefore, that said document constituted the return required by law. More than five years having elapsed subsequent to the filing of said return and prior to the mailing of the deficiency notice, it follows that assessment and collection of the proposed deficiency are barred by limitation."

Indiana Rolling Mills Co. vs. Commissioner, 13 B. T. A. 1141.

The filing of a consolidated return on behalf of a group of associated corporations, which was neither false nor fraudulent, has been held to be the return of each of said corporations and sufficient to start the running of the limitations in Section 277 (a) (2) of the Revenue Act of 1924, although the corporation later filed separate returns.

Kellogg Commission Co. vs. Commissioner, 6 B. T. A. 771, Acquiesced in by Commissioner, Cum. Bull. VII, 1, p. 17.

Fibre Container Co. v. Commissioner, 9 B. T. A. 575, Acquisced in by Commissioner, Cum. Bull. VII, 1 p. 10.

Appeal of F. A. Hall Co., 3 B. T. A. 1172, Aquiesced in by Commissioner, Cum. Bull. VII, 1, p. 13.

Appeal of National Tank & Export Co., 3 B. T. A. 1217.

I. T. 2451—Int. Rev. Bull. VIII-4-4082.

A consolidated return filed in good faith by the taxpayer, which separately showed the assets and liabilities of each corporation, but did not show separately the items of income and deductions applicable to each corporation, has been held sufficient to start the running of the Statute of Limitations, although separate returns should have been filed.

Colmer-Green Lumber Co., 12 B. T. A. 256.

The filing of a consolidated return by several corporations, where separate returns should have been filed, has been held to start the running of the Statute of Limitations and to substantially conform to the statute requiring returns, notwithstanding the consolidated return did not set forth sufficient details to accurately compute the tax against each corporation, and in connection with that holding the Board of Tax Appeals said:

> "The rule which the Board has laid down in cases similar to the instant case, if there can be said to be a rule governing all cases, is that there must be a 'substantial' compliance with section 239, *supra*. What constitutes a substantial compliance must necessarily vary according to the circumstances in each individual case. To require a literal compliance with Section 239, *supra*, such as the respondent would have us do, would relegate the limitations provisions of the statutes to the discard." • • •

"Where a consolidated return has been prepared and filed in good faith, and the names of the companies included in the consolidation are made clear to the respondent, and all of the 'items of gross income and the deductions' are included therein, although said items of income and deductions may not be in sufficient detail to enable the respondent to accurately compute the tax against each of the companies, there is a 'substantial' compliance with the statute."

Stetson & Ellison v. Commissioner, 11 B. T. A. 397.

The corporate taxpayer kept its books upon a fiscal year basis ending January 31, but filed its returns on a calendar year basis for the years 1918 and 1919. The returns filed June 5th, 1919, and February 24th, 1920, on the calendar year basis gave the Commissioner of Internal Revenue information as to the entire period covered by the fiscal year ending January 31, 1919, and it was held that the return filed February 24th, 1920, started the running of the Statute of Limitations upon the collection of a deficiency in the tax for the fiscal year ending January 31, 1919, and that proceedings to collect the tax begun more than five years after that date, were barred by Section 277 (a) (2) of the Revenue Act of 1924.

Lowenstein Bros. Garment Co. 13 B. T. A. 446.

See Also:

Paso Rables Mercantile Co., 12 B. T. A. 750.

Willingham L. & T. Co., 15 B. T. A. 931.

The erroneous computation of the tax by a taxpayer upon a return made upon a calendar year basis instead of upon a fiscal year basis does not destroy the effect of the return, in starting the running of limitation provisions.

Appeal of Washburn, 7 B. T. A. 438, acquiesced in by Commissioner, Cum. Bull. VII, 1, p. 33.

The entire failure of the taxpayer to compute the tax upon the return does not destroy the effect of the return, for the same purpose.

Conrad Hardware Co. vs. Commissioner, 8 B. T. A. 512. Acquiesced in by Commissioner, Cum. Bull. VII, 1, p. 7.

In the Conrad Hardware Company case, the taxpayer filed a return for a fiscal period ending in 1920 upon Form 1120-A, which was intended to cover fiscal years ending during a year prior thereto, and did not contain items for a correct computation of the tax under the 1918 Act. These items were left blank by the taxpayer. The collector did not forward this return to the Commissioner of Internal Revenue, but returned same to the taxpayer with Form 1120, requesting that the taxpayer's return be made upon the other form. The taxpayer retained the first return and filled out the second return, upon which he calculated the tax and then filed it with the collector. After five years from the filing of the first return, but within five years from the filing of the second return, the Commissioner proceeded to assess and collect a deficiency. The Board of Tax Appeals held that the five-year period

prescribed in Section 250 (d) of the Revenue Act of 1921 started to run from the date of the filing of the first return, and in that connection said:

> "The Commissioner insists that because the return executed October 26, 1920, and transmitted to the collector for filing and received and stamped by the collector, was not retained by him, it was not 'filed' and did not operate to start the running of the statute of limitations within which assessment and collection of any tax for the fiscal year ending August 31, 1920, might be made. He says that this return was not received by him and that he cannot be charged with knowledge that it was received by the collector; that he could not examine the return as required by section 250 of the Revenue Act of 1918 because it was never in his custody. * * * The collector should not have sent the return back to the petitioner. All that remained to be done upon the return which the petitioner filed was to compute the tax at the rates provided by the Revenue Act of 1918, upon the net income shown in the return. While there is no direct evidence on this point, it would appear probable that the reason the collector sent the first return back to the petitioner was because it had been made on a form which contained in 'Schedule V—Computation of taxes' rates to be used in determining the amount of tax for a fiscal year beginning in 1918 and ending in 1919, and that evidently accounts for the fact that petitioner did not make a computation of the tax upon this return. The running of the statute of limitation, however, does not depend upon whether the taxpayer computed the tax upon the income shown on the return made to the collector. The fact that the return is inaccurate or that it is filed on a calendar year instead of a fiscal year basis does not postpone the date on which the statute of limitation begins to run. See *Appeal of Mable Elevator Co.*, 2 B. T. A. 517; *United States vs. Mable Elevator Co.*, 17 Fed. (2nd) 109."

It has been further held that the filing of a joint return by husband and wife as required by treasury regulations then existing, started the running of the statute of limitations upon a deficiency against the wife, notwithstanding the husband and wife later filed separate returns to take advantage of a right subsequently granted to file separate returns, whereby the amount of their taxes would be reduced.

Thomas v. United States, 22 Fed. (2nd) 1000 (D. C. N. D. Tex.)

All of the above holdings are in keeping with the principle announced in *Tucker vs. Alexander,* 25 Fed. (2d) 425, wherein it is said:

"Substance and not form must govern in constructing and applying income tax laws."

Citing *U. S. vs. Phellis,* 257 U. S. 156.

(b)

Was "A Return" Made and Filed by the Commissioner of Internal Revenue?

Section 14 (a) of the Revenue Act of 1916 (39 Stat. 772):

"* * * That every corporation, * * * computing taxes upon the income of the fiscal year which it may designate in the manner hereinbefore provided, shall pay the taxes due under its assessment within one hundred and five days after the date upon which it is required to file its list or return of income for assessment; except in cases of refusal or neglect to make such return, * * * in which cases the Commissioner of Internal Revenue shall, upon the discovery thereof, at any time within three years after said return is due,

make a return upon information obtained as provided for in this title or by existing law; * * * *Provided,* That upon the examination of any return of income made pursuant to this title, * * * if it shall appear that amounts of tax have been paid in excess of those properly due, the taxpayer shall be permitted to present a claim for refund thereof notwithstanding the provisions of section thirty-two hundred and twenty-eight of the Revised Statutes;"

Section 14 (b) of the Revenue Act of 1916 (39 Stat. 772):

"When the assessment shall be made, as provided in this title, the returns, together with any corrections thereof which may have been made by the commissioner, shall be filed in the office of the Commissioner of Internal Revenue * * * "

The same authority to the Commissioner to make returns is found in various regulations in force at the time the Commissioner made returns in the instant case, particularly in the following:

Regulation 33, Article 177.

Regulation 33, Article 184.

Regulation 33 (Revised), Article 42, Paragraph 253.

If it is claimed that the returns made and filed by the taxpayers were not accepted or adopted by the Commissioner as returns under the October 3d, 1917 Act, and for the assessment of the additional tax under said Act, then we contend that the returns prepared by the Commissioner of Internal Revenue through the revenue agent and revenue agent in charge at Omaha in October, 1918,

and forwarded to the Commissioner of Internal Revenue by the revenue agent in charge under date of October 26th, 1918, and stamped "Return Audited," was "a return" within the meaning of Section 278 (a) of the 1924 and 1926 Acts. Such returns were not required to be subscribed by the Commissioner at the time same were made and filed, as was the case of returns made by the collector or deputy collector of Internal Revenue, or as was afterwards required with respect to returns made by the Commissioner.

Other Limitation Provisions.

If it is claimed that this case does not come within the provisions of Section 277 or Sections 278 of the Revenue Act of 1926, then it must be governed by Section 1109 (a) (1), (2) and (3), (44 Stat. 114), which is the dragnet limitation section intended to cover all cases for which there is no specific provision. The sub-divisions of this section are as follows:

"(a) Except as provided in sections 277, 278, 310 and 311—

"(1) Notwithstanding the provisions of section 3182 of the Revised Statutes or any other provision of law, all internal-revenue taxes shall (except as provided in paragraph (2) or (3) of this subdivision) be assessed within four years after such taxes became due, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of five years after such taxes became due.

"(2) In case of a false or fraudulent return with intent to evade tax, of a failure to file a return within the time required by law, or of a willful attempt in any manner to defeat or evade tax, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment at any time.

"(3) Where the assessment of any tax imposed by this Act or by prior Act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (A) within six years after the assessment of the tax, or (B) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer."

III.

The lawful distribution of the assets of a corporation in August, 1917, when no debts, or obligations of any kind then existing, remained unpaid, could not become unlawful by subsequent legislation. A subsequent creditor, even when the creditor is the government, cannot question a lawful distribution by a corporation to its stockholders, whether of dividend or of capital.

It is alleged, both in the petition and in the answer, (R. 9-13), that in August, 1917, before the passage of the law in question, this corporation by due action of its stockholders had decided upon the formal dissolution, and had arranged for converting its assets into money for convenient distribution, and in the language of the plaintiff's bill, (R. 10) its assets were "forthwith and prior to the date of its formal dissolution by it, distributed among its stockholders, the above named defendants, ratably according to their stockholdings of its shares of stock."

It is alleged in the answer and shown in the evidence that at the time this distribution was made, all the debts and taxes of every kind had been paid, so that on the first day of August, 1917, the corporation was not indebted to any existing creditor, whether on a matured or inchoate debt of any kind. The distribution of assets was lawful as against all existing claimants, because they were all paid.

There is no claim that the stockholders were liable on any liability created by state statute. There were no unpaid stock subscriptions. There was no state law, imposing a liability on stockholders for non-compliance,

which had not been fully complied with. Conversely, the Revenue Acts nowhere make the stockholders of any corporation personally liable for corporate tax.

There is, therefore, no theory of liability which can apply to these defendants, except that which regards them as voluntary transferees, liable as such under state or general law.

The position of the Government in this suit, therefore, is that of a subsequent creditor, seeking to set aside a prior transfer of property upon the ground that it was unlawful. There is no warrant of law for maintaining such a claim. It is well settled that as against a distribution of property by a corporation, whether by way of dividend or of capital assets, only existing creditors can enter their protest and enforce it by legal proceedings. Subsequent creditors who become such after the distribution of assets have no standing in a court of equity to complain of the lawful actions which took place before their claim came into existence.

And this is true, even though it should be held by this court that a lawful tax was levied upon the corporation as such, and that the corporation as an entity, having whatever projected existence might be given to such a corporation after its dissolution, became technically liable to the payment of the tax by the subsequent legislation and the subsequent assessment of a tax against it under such subsequent statute.

The case in that respect is precisely analagous to that of an individual who for any cause might give away

his property or distribute it among his relatives at a time when he is not indebted to any one and is not contemplating any debt. If he should subsequently become indebted or, as in this case, if legislation should subsequently create against him a liability for a tax, which as we shall see in the case of the income tax is purely a personal obligation and is not a tax *in rem* against any property, this personal obligation cannot be satisfied out of the property which he had transferred in good faith before the obligation came into existence. This rule as to individuals has been expressly held by this court to be applicable to corporations. In such cases this court has rejected the so-called "trust doctrine" by which alone the property of a solvent corporation can be deemed to be held in trust for future creditors.

In the case of *Graham v. Railroad Company*, 102 U. S. 148, the court holds that the disposition by a corporation of any of its property cannot be questioned by subsequent creditors of the corporation any more than a like disposition of property by an individual can be.

In this case it was charged that the corporation had indirectly sold its property to its directors or officers for an inadequate consideration and that in any case the transfer was technically voidable. The suit was brought by a subsequent creditor to subject the property to a judgment upon a claim arising subsequent to the transfer of the property. After announcing the rule that the creditor of an individual cannot question transfers taking place before the inception of the debt, the court holds that the same rule applies to a corporation. It was contended

by the creditor that the doctrine of the trust fund would apply to such a case, but the court says:

> "We do not concur in this view. It is at war with the notions which we derive from the English law with regard to the nature of corporate bodies. A corporation is a distinct entity. Its affairs are necessarily managed by officers and agents, it is true; but, in law, it is as distinct a being as an individual is and is entitled to hold property, if not contrary to its charter, as absolutely as an individual can hold it. Its estate is the same, its interest is the same, its possession is the same. Its stockholders may call the officers to account, and may prevent any malversation of funds or fraudulent disposal of property on their part. But that is done in the exercise of their corporate rights, not adverse to the corporate interests, but coincident with them.
>
> "When a corporation becomes insolvent, it is so far civilly dead that its property may be administered as a trust fund for the benefit of its stockholders and creditors. A court of equity, at the instance of the proper parties, will then make those funds trust funds, which, in other circumstances, are as much the absolute property of the corporation as any man's property is his. We see no reason why the disposal by a corporation of any of its property should be questioned by subsequent creditors of the corporation, any more than a like disposal by an individual of his property should be so. The same principles of law apply to each."

In the case of *Hollins v. Brierfield Coal & Iron Co.*, 150 U. S. 371, in holding that simple contract creditors could not maintain a bill in equity to satisfy their claims from the property of a corporation, the court again discusses the doctrine of the trust fund and holds that it has no existence when applied to a corporation which is

solvent at the time of the transaction under attack. The trust arises only when the corporation is insolvent and is being administered in equity for the benefit of its creditors. The court cites with approval the opinion in *Graham v. Railroad Company,* quoted above. In addition, it says:

> "In other words, and that is the idea which underlies all these expressions in reference to 'trust' in connection with the property of a corporation, the corporation is an entity, distinct from its stockholders as from its creditors. Solvent, it holds its property as any individual holds his, free from the touch of a creditor who has acquired no lien; free also from the touch of a stockohlder, who, though equitably interested in, has no legal right to the property. Becoming insolvent, the equitable interest of the stockholders in the property, together with their conditional liability to the creditors, place the property in a condition of trust, first, for the creditors, and then for the stockholders. Whatever of trust there is arises from the peculiar and diverse equitable rights of the stockholders as against the corporation in its property and their conditional liability to its creditors. It is rather a trust in the administration of the assets after possession by a court of equity than a trust attaching to the property, as such, for the direct benefit of either creditor or stockholder."

Again the court says:

> "A party may deal with a corporation in respect to its property in the same manner as with an individual owner, and with no greater danger of being held to have received into his possession property burdened with a trust or lien. The officers of a corporation act in a fiduciary capacity in respect to its property in their hands, and may be called to an account for fraud or sometimes even mere mismanagement in respect thereto; but as between itself and

its creditors the corporation is simply a debtor, and does not hold its property in trust or subject to a lien in their favor, in any other sense than does an individual debtor. * * * Neither the insolvency of the corporation, nor the execution of an illegal trust deed, nor the failure to collect in full all stock subscriptions, nor all together, gave to these simple contract creditors any lien upon the property of the corporation, nor charged any direct trust thereon."

In *Leudecke v. Des Moines Cabinet Co.*, 140 Ia. 223; it is said of the so-called trust doctrine in relation to the assets of a solvent corporation:

"While at one time quite generally adopted in this country, it is now believed to be unsupported to its full extent by any considerable number of courts. Indeed, the court which first announced it has largely receded from its former position, and now says that no trust in its true sense exists; that all that was intended by the previous expressions was to announce the existence of an equitable right, which will be enforced whenever a court of equity, at the instance of a proper party, has taken possession of its assets,"

citing in support of this position the case of *Hollins v. Coal Co.*, 150 U. S. 371, cited above.

The Iowa court further says:

"We have recently gone over this matter in the case of *State Trust Co. v. Turner*, 111 Iowa 664; 82 N. W. 1029, and have repudiated the trust-fund doctrine as broadly announced in some of the earlier cases in this country."

But the Iowa court held in the case before it in favor of a pre-existing creditor, that a transfer of all the assets of the company was subject to the claim of such

creditor and in a suit in equity to enforce his claim, he was entitled to a lien upon such transferred assets.

In *McDonald v. Williams,* 174 U. S. 397; this court held that the receiver of a national bank cannot recover back from a stockholder a dividend paid him although it was paid out of the capital, and was paid prior to the appointment of a receiver, when such stockholder receiving such dividends acted in good faith, believing the same to be paid out of the profits made by the bank, and the bank at the time of the payment of the dividend was solvent.

In this case there was a distribution of capital under the pretense of paying a dividend which had not been earned. But the bank was solvent, and although it subsequently became insolvent and was placed in the hands of a receiver representing, of course, subsequent crditors, such receiver had no standing to recover back the assets from the stockholder.

The court cites in support of its decision the case of *Graham v. Railroad Company,* 102 U. S. 148, which we have already cited, and *Hollins v. Brierfield Coal & Iron Company,* 150 U. S. 371, cited above, and says:

> "These cases, while not involving precisely the same question now before us, show there is no well-defined lien of creditors upon the capital of a corporation while the latter is a solvent and going concern, so as to permit creditors to question, at the time, the disposition of the property.
>
> "The bank being solvent, although it paid its dividends out of capital, did not pay them out of a trust fund. Upon the subsequent insolvency of the

bank and the appointment of a receiver, an action could not be brought by the latter to recover the dividends thus paid on the theory that they were paid from a trust fund, and therefore were liable to be recovered back.

"It is contended on the part of the complainant, however, that if the assets of the bank are impressed with a trust in favor of its creditors when it is insolvent, they must be impressed with the same trust when it is solvent; that the mere fact that the value of the assets of the corporation has sunk below the amount of its debts, although as yet unknown to anybody, cannot possibly make a new contract between the corporation and its creditors. In case of insolvency, however, the recovery of the money paid in the ordinary way without condition is allowed, not on the ground of contract to repay, but because the money thus paid was in equity the money of the creditor; that it did not belong to the bank, and the bank in paying could bestow no title in the money it paid to one who did not receive it bona fide and for value. The assets of the bank while it is solvent may clearly not be impressed with a trust in favor of creditors, and yet that trust may be created by the very fact of the insolvency and the trust enforced by a receiver as the representative of all the creditors. But we do not wish to be understood as deciding that the doctrine of a trust fund does in truth extend to a shareholder receiving a dividend, in good faith believing it is paid out of profits, even though the bank at the time of the payment be in fact insolvent. That question is not herein presented to us, and we express no opinion in regard to it. We only say that if such a dividend be recoverable, it would be on the principle of a trust fund.

"Insolvency is a most important and material fact, not only with individuals but with corporations, and with the latter as with the former the mere fact of its existence may change radically and materially its rights and obligations. * * * Although no

trust exists while the corporation is solvent, the fact which creates the trust is the insolvency, and when that fact is established at that instant the trust arises. To prove the instant of creation may be almost impossible and yet its existence at some time may very easily be proved. What the precise nature and extent of the trust is even in such case may be somewhat difficult to accurately define, but it may be admitted in some form and to some extent to exist in a case of insolvency.

"Hence, it must be admitted that the law does create a distinction between solvency and insolvency, and that from the moment when the latter condition is established the legality of acts thereafter performed will be decided by very different principles than in a case of solvency. * * * The fact of insolvency must be proved in order to show the act was one committed in contempation thereof."

In *Sexton v. Wheaton,* 8 Wheaton 229; the leading case on the rights of subsequent creditors, this court held that a post-nuptial voluntary settlement made by a husband, who is not indebted at the time, upon his wife, is valid against subsequent creditors, holding that the Statute 13 Eliz. c. 5, then in force, avoids all conveyances not made on a consideration deemed valuable in law, as against previous creditors, but does not apply to subsequent creditors if the conveyance is not made with a fraudulent intent. Chief Justice Marshall, in his opinion, points out that the bill does not charge the husband was indebted when the conveyance was made, and the fact that he subsequently was insolvent is no ground for assuming that he was in that condition at the time of the conveyance, and says:

> "It would seem to be a consequence of that absolute power which a man possesses over his own property, that he may make any disposition of it which does not interfere with the existing rights of others, and such disposition, if it be fair and real, will be valid. The limitations on this power are those only which are prescribed by law."

The court then discusses the statute against fraudulent conveyances above cited and holds that the courts have considered every conveyance not made on consideration admittedly valuable in law as void against previous creditors, and this application to subsequent creditors has been in doubt in some cases, which the court then proceeds fully to analyze with the result of holding that a subsequent creditor whose claim was not in contemplation at the time of the transfer has no standing to question the conveyance.

In *Mattingly v. Nye,* 8 Wall. 370; an identical case was decided in the same way, the court holding that a settlement by a husband for his family was unaffected as to subsequent creditors by the statute against fraudulent conveyances, unless fraud was intended at the time of the transfer; citing *Sexton v. Wheaton,* 8 Wheaton 229, and suggesting that the whole learning of the law upon this subject is so fully developed in that case that further discussion is unnecessary.

In *Lawrence v. Greenup,* 97 Fed. 906, 6th C. C. A., the opinion is by Mr. Justice Lurton and it was concurred in by Justices Taft and Swan. The holding of the court is clearly stated in the syllabus, which is as follows:

"Under the decisions of the courts of the United States, a solvent corporation does not hold its capital or property subject to any trust in favor of its creditors, although it is in process of liquidation.

"The receiver of a national bank cannot recover from a stockholder, in an action at law, a sum received by him on a partial distribution of the capital of the bank, made and received in good faith during voluntary liquidation, when the bank was at the time solvent, and retained sufficient assets to pay all its liabilities, although it subsequently became insolvent."

Of course these ancient cases are the leading cases on this question and have never since been challenged in any subsequent decisions in the Federal or state courts; and they apply to the case now before the court.

The decisions of the Supreme Court of Nebraska are in line with the Supreme Court of the United States on the trust fund doctrine.

In *Shaw v. Robinson & Stokes,* 50 Neb. 403, the Nebraska court held that there is no general rule that the assets of a corporation are held in trust for its creditors and that even when it is insolvent it has a right to prefer some of its creditors over others, which of course it could not do if the property were held in trust for all creditors in any specific sense. In reaching this conclusion, the Nebraska court quotes with approval the decision in *Hollins v. Coal Company,* 150 U. S. 371, cited above, and states that it approves the ruling announced in the case of *Hospes v. Northwestern Manufacturing Company,* 48 Minn. 174; where it is said:

"The capital of a corporation is its property. It has the whole beneficial interest in it, as well as the legal title. It may use the income and profits of it, and sell and dispose of it the same as a natural person. It is a trustee for its creditors in the same sense, and to the same extent as a natural person, but no further."

It is to be noted that none of the statutes providing for income or excess profit taxes makes the taxes a lien upon the property of the taxpayer, but each of them contains a clause to the effect that all of the provisions of the general revenue law for the collection and enforcement of taxes are available, and Section 3186 of the Revised Statutes provides that taxes become a lien upon the property of the taxpayer only when the assessment list is received by the Collector.

In the following recent cases, under varying state statutes, enacted upon the basis of the statute of 13th Elizabeth, it has been held that creditors not existing at the time of the transfer by individuals of their property to voluntary transferees, without consideration, cannot set aside the transfer by a creditor's bill, or pursue the assets by any form of proceeding, where the creditor's claim did not exist at the time of the claim. *Old Grove Church v. Rice,* 162 Ky. 525; *Clement v. Bank,* 115 Tex. 342; *Washington Bank v. Beatty,* 77 N. J. E. 252; *Farmers Bank v. Daiker,* 166 Ia. 728; *Coulter v. Meining,* 143 Minn. 104; *Crowley v. Brower,* 201 Ia. 257; *Parker v. Hand,* 299 Ill. 420; *Powell v. Gallivan,* 44 R. I. 453; *Aldrich v. Van Hemert,* 205 Ia. 460.

The ruling in those cases is not announced as a new or untried principle of law, but referred to through-

out the discussion in the decisions as well settled and long established.

And in recent decisions of the United States courts, the foregoing rule has been made applicable to transfer by corporations of their assets to their stockholders. *Radcliffe v. Clendenin,* 232 Fed. 61 (8th C. C. A.); *Sweet v. Lang,* 14 Fed. (2d) 762 (8th C. C. A.); *Wood v. Bank,* 24 Fed. (2d) 661 (2d C. C. A.).

In 1884 this court held, in a case arising under Nebraska law, *Horbach v. Hill,* 112 U. S. 144, that a creditor cannot, by a creditor's bill, successfully attack and set aside a conveyance of the debtor made at a time prior to the existence of the creditor's claim, this court saying that, "Even a voluntary conveyance is good as against subsequent creditors, unless executed as a cover for future schemes of fraud."

IV.

The act of October 3rd, 1917, does not authorize a levy of taxes for incomes and excess profits upon stockholders of corporations existing during a portion of the year, where such corporations were dissolved, and had wound up their affairs, paid all existing obligations and distributed all their property among their stockholders prior to the passage of the act.

The statute is Chapter 63, Volume 40, Part I, United States Statutes at Large, Pages 300-338. Title I provides for an increase in the income taxes in the Act of September, 1916, Title 2 provides for the war excess profits tax and repeals the Act of March, 1917. Other titles in the Act provide for taxes on beverages, tobacco, public utilities and insurance, war excise taxes on admissions and dues, stamp taxes, estate tax, and an increase in postal rates, and amends in many respects the administrative provisions of the preceding income tax statutes. Its concluding section (page 338) is as follows:

> "Sec. 1302. That unless otherwise herein specially provided, this Act shall take effect on the day following its passage."

It was passed October 3, 1917. In Section 200, page 302, occurs the following language:

> "The term 'taxable year' means the twelve months ending December thirty-first, excepting in the case of a corporation or partnership which has fixed its own fiscal year, in which case it means such fiscal year. The first taxable year shall be the year ending December thirty-first, nineteen hundred and seventeen, except that in the case of a corporation or partnership which has fixed its own fiscal year, it shall be the fiscal year ending during the calendar year nineteen hundred and seventeen."

When this statute came before the Commissioner of Internal Revenue for construction and enforcement, the first holding there was to the effect that it did not apply to dissolved corporations. By letter written by Deputy Commissioner L. F. Speer, to two taxpayers in New York, dated October 7, 1917, it is held that a corporation dissolved in June, 1917, was subject to tax under the Act of September, 1916, and under the Act of March, 1917, but would not be subject to the tax imposed by the Act of October 3, 1917, for the reason that the Government cannot revive a dead corporation in order to assess taxes which are imposed by laws enacted subsequent to the dissolution of the corporation.

But by letter of November 17, 1917, signed by Commissioner D. C. Roper, this ruling was reviewed and it was held upon the authority of *Brady v. Anderson*, 240 Federal 665, that a corporation which was dissolved during the year 1917, prior to the approval of the Act of October 3, 1917, is subject to the taxes imposed by that Act. It was held that such corporation should file a return in accordance with the provisions of the later Act and pay the taxes imposed by it.

The dissolution of a corporation under Nebraska law and its status upon dissolution.

The statutes of Nebraska provide that corporations may be organized by any number of persons for the transaction of any lawful business by adopting articles of incorporation, setting forth certain of the powers and limitations of the corporation, and filing the articles in the office of the Secretary of State and the County Clerk of the county where the business is to be conducted, and

publishing a notice in a newspaper for a period of four weeks. (Chap. 12, Art. 2, Compiled Statutes of Nebraska, 1922.)

The provisions for the dissolution of solvent corporations are contained in the following sections of the Nebraska statute, found in the Compiled Statutes of Nebraska for 1922, but in operation prior to and during the year 1917:

> "Sec. 468. No corporation can be dissolved by the members thereof except by consent of two-thirds of all its members, which consent must be entered on its records, unless a different rule has been adopted in its articles of incorporation."

> "Sec. 700. Each domestic corporation in case of dissolution or revocation of its charter shall file with the Secretary of State a certificate of such dissolution or revocation of its charter; in case of dissolution by voluntary action of the corporation, such certificate shall be signed by the president and secretary of the corporation. * * *"

Other portions of the statute following the above sections provide that in the case of dissolution, the title of any property remaining in the corporation at the time of its dissolution becomes vested in the directors, who are made trustees, and who are charged with the duty of paying the debts and meeting the obligations existing against the corporation at the time of its dissolution. These provisions have no application to the case of the corporation we are considering, for the reason that all the obligations of this corporation, including taxes arising under the Act of March, 1917, and the prior Acts, had been fully satisfied, and all the assets remaining after such payment were

distributed among the stockholders, so that the trust provided for by the statute never arose in this case. But, even if it had, it would have ceased to exist before the passage of the Act, because the trustees are created by statute, no order of any court is invoked for their appointment, and they do not remain in office until discharged by the court; the termination of the trust would of itself terminate their trusteeship.

The nature of the income tax. It is a personal tax, not a tax in rem.

It becomes important in this connection to consider the nature of the income tax, whether it is a tax upon property or a tax upon a taxpayer with respect to income received by him during a specified period.

The question here is not whether the tax is direct or indirect. In *Pollock v. Farmers Loan & Trust Company*, 157 U. S. 429, 158 U. S. 601, in which the income tax law of August 15, 1894, was held invalid, the controversy was whether the income tax is a direct or indirect tax. But this distinction is not the same as between a specific tax upon property and a tax upon a taxpayer. Capitation taxes are also direct taxes, but they are not specific taxes levied *in rem* upon the property itself.

In *Brady v. Anderson*, 240 Federal 665, the Circuit Court of Appeals held that the tax was personal and not *in rem*:

> "In our opinion the tax is against the citizens and residents of the United States personally. They are chargeable in respect to income received by them. The statement that the tax is upon this income does

not create an obligation *in rem*. It is only a way of saying that the owner is taxable with reference to the income. Taxable persons are spoken of throughout the act."

Likewise, in *Smietanka v. First Trust & Savings Bank*, 257 U. S. 602, in holding that under the terms of the income tax law of 1913, income held by a trustee for the benefit of unborn and unknown beneficiaries was not taxable, this Court said:

> "There must have been a taxable person for whom the fiduciary was acting to make the provisions relied upon by the government applicable."

As the court says in the same opinion, the tax is upon "persons natural and corporate."

The Act of October 3rd, 1917, applies only to taxpayers existing at the time of the passage of the Act or thereafter coming into existence, or representatives, specified in the Act itself, of taxpayers who had become non-existent when the Act was passed.

If the tax is upon the corporation and not *in rem*, upon the income as property, then before the taxing officers of the Government can demand the payment of a tax from an individual taxpayer, they must point out the provision in the statute which justifies the demand. At the time of the passage of the Act, this corporation was not in existence. We have seen that under the Nebraska statute, having met all existing obligations and distributed all its property, it was as completely out of existence as if it had never been organized. Congress could tax it by a tax levied *in personam*, and not *in rem*, only by bringing back into existence the creation of the

statute of Nebraska, which by operation of the laws of that state had ceased to have any existence for any purpose whatsoever. This Congress has no power to do. Congress can doubtless create Federal corporations for Federal purposes, but it cannot create state corporations for the sole purpose of taxing them.

The stockholders of the dissolved corporation were in existence, and were the owners of the income or of the property into which the income had been converted, upon which it is sought to levy this tax. The stockholders could have been taxed, and could have been taxed with respect to the income which had wholly accrued and been distributed among them prior to the passage of the Act.

But Congress has failed in the Act of October 3, 1917, to provide that the stockholders of a dissolved corporation shall be charged personally with income received by them from the dissolved corporation upon the same basis as the corporation would have been taxed if it were in existence at the time the law was enacted. Parenthetically, it may be said that each stockholder incurred liability for taxation under this and previous laws, by receiving from the corporation the income in the form of dividends, but that liability was fully met by the stockholders in their individual returns and is not now in issue.

The real question, therefore, is not whether this law is retroactive with respect to income which accrued prior to its passage, and if it is, whether such retroactive effect invalidates its provisions in that respect; but is rather whether by the terms of the Act itself the tax is levied

upon the only existing representatives of the corporation who received the income.

While by the provisions of the Nebraska statute which have been cited, the directors of a dissolved corporation become trustees and are vested with the title to its property, and are charged with the duty of liquidating its affairs and made liable for its debts to the extent of assets received by them, yet even that trust had wholly ceased in this case, because upon the payment of the debts and the distribution of all the assets, the trust itself, together with the existence of the corporation, would cease to exist. While the statute provides that the trustees shall be subject to control of the court and may be sued in equity on behalf of any person interested, on account of any neglect or omission of duty or abuse of trust, and in case of their removal the court may appoint other trustees to fill the vacancy, yet as these trustees are created by general law, and are not appointed by any court in pending proceedings, they do not remain in office until discharged by a court. The trust ceases when the subject matter of the trust no longer exists.

Can it be said that the failure of the statutory trustees of these corporations to foresee in August the passage of the tax law in October, and retain sufficient property of the companies to pay the tax, was a breach of trust?

Nor can it be said that the provisions in the state statute to the effect that a dissolved corporation may be sued at law or in equity by its corporate name on account of any cause of action which accrued, or but for such dissolution would have accrued against the corpora-

tion if it had not been dissolved, will have the effect of making these corporations in existence *pro tanto*, for the purpose of being subject to the tax established by Congress under the Act of October 3, 1917, after the dissolution of the corporation and the termination of the trust accruing out of it. It was obviously the intention of the state statute, in line with similar statutes in other states, to abrogate the narrow rule of the common law, by which upon the dissolution of a corporation, all its debts were cancelled and all its obligations ceased to exist. *Mumma v. Potomac*, 8th Pet. 281; *McRae v. Kansas City Piano Co.*, 69 Kans. 457; *Clark v. American Can. Coal Co.*, 165 Ind. 213.

But although the state statute was intended to modify the law of corporations in a manner consistent with the financial and commercial purposes for which they are now used, it could not be contended that the legislature of Nebraska had any intent to keep alive the existence of these dissolved corporations, for the purpose of making effective any statute which the Congress of the United States might thereafter enact for levying taxes upon existing corporations.

It was not the intention of the state statute to keep alive these corporations, for the sole purpose of Federal taxation, after they had ceased to exist for any other purpose.

The foregoing suggestions would apply to a case in which at the time of the dissolution the corporation still retained some of its property, and had obligations of some character which required auditing, adjusting and

settling. But in the case of these corporations we are considering, all such arrangements were made before the dissolution. It is competent for a Nebraska corporation under Nebraska statutes to distribute all its property among its stockholders, after having met all its obligations, and then when it remains only a dry shell, to complete the process of dissolution by filing a certificate in the office of the Secretary of State, with the authority of two-thirds of its stockholders. When this step is taken, it cannot be said that the directors or other officers of the corporation ever became trustees or that any trust exists for any purpose. The statute regarding the trust imposed upon the officers was designed to take care of a situation in which property remains in the corporation at the time of its dissolution and obligations may exist with reference to it. But it is clear that if there is no property and no existing obligations there is no trust.

It is apparent, therefore, that before this tax can be incurred, it is necessary to find in this Act a provision that it applies to corporations which had ceased to exist at the time it was enacted, or that the tax which would have been assessed against corporations if they had existed, is by the law levied upon the stockholders who were in existence when the law was passed, and who had received the distributed assets of the corporation.

No tax can be levied by the Treasury Department under the general provisions of the Act, unless there is found specific language applicable to the alleged taxpayer.

In *Smietanka v. First Trust & Savings Bank,* 257 U. S. 602, the language of this court, and its rulings and decision, would seem to overturn the effect

of the cases in the lower courts heretofore relied on by the Government.

In that case, the Government sought to collect an income tax from a trustee in a trust created by a will, which provided that the income of the estate should be accumulated by the trustee and thereafter distributed among the beneficiaries who, at the time of the creation of the trust, might be unborn or unascertained.

In the opinion of the Chief Justice, it is said:

> "There was nowhere in the Act a payment required of the fiduciary of a tax upon the income of the estate or trust property, the income from which he collects, except as it is to inure to the benefit of a person or an individual from whose income he is authorized and required to deduct the normal tax thereon. There must have been a taxable person for whom the fiduciary was acting to make the provisions relied upon by the Government applicable."

After pointing out that the Treasury Department did not attempt for two years to collect the tax in question and thereafter by a change in its rulings had sought to do so and adopted a regulation which would compel the payment of the tax, the court says:

> "This seems to us to graft something on the statute that is not there. It is an amendment, and not a construction."

In the case of *Gould v. Gould*, 245 U. S. 151, this court held that alimony paid to a divorced wife, under a decree of court, is not subject to income tax, under the Act of October 3, 1913, notwithstanding the broad

language of that Act, for the reason that there was no express provision that alimony should be deemed income.

In so holding, the court said:

> "In the interpretation of statutes levying taxes, it is the established rule not to extend their provisions by implication beyond the clear import of the language used; or to enlarge their operations so as to embrace matters not specifically pointed out. In case of doubt, they are construed most strongly against the Government and in favor of the citizen."

In the case of *Scott v. Railroad Company,* 246 Fed. 545, the Court of Appeals of the Ninth Circuit held that under the Act of October 3, 1913, no income tax was payable by a corporation in the hands of a receiver, for the reason that such cases were not covered by that Act, although it contained the same general language levying a tax upon all income and although there was a receiver in existence capable of representing the corporation, and the court held that the provision in the Act of 1913, requiring receivers to make returns and pay tax, was applicable only to receivers for persons, since there was a failure to mention receivers for corporations in the section of the statute relied upon by the Government.

Where a revenue statute is of doubtful construction, the doubt must be resolved in favor of the taxpayer and a liberal construction must be given words of exception confining the operation of duty; and before the property of the citizen can be taken for revenue, the statute must be clear and unambiguous.

Schwab v. Doyle, Collector, 258 U. S. 529, is one of the latest utterances of this court on this point. There the holding of the court was that transfers or trusts made or created prior to the Act of September 8, 1916, are not comprehended by the provisions of that Act imposing a tax upon the transfer of the net estate of every decedent dying after the passage of that Act, to the extent of any interest therein of which the decedent has at any time made a transfer, or with respect to which he has created a trust in contemplation of, or intended to take effect in possession or enjoyment, at or after his death, except in case of a *bona fide* sale, and creating a presumption that transfers without consideration within two years prior to death are to be deemed made in contemplation of death. After holding with reference to retrospective laws, that the same principle which absolutely prohibits them when their purpose is punitive, exacts clearness of declaration when burdens are imposed upon completed and remote transactions, or consequences given to them of which there could have been no foresight or contemplation when they were designed and consummated, Mr. Justice McKenna, speaking for the court, said:

> "The Act of September 8, 1916, is within the condemnation.
>
> "There is certainly in it no declaration of retroactivity, 'clear, strong, and imperative,' which is the condition expressed in *United States v. Heth,* 3 Cranch, 398, 413, 2 L. ed. 479, 483, also *United States v. Burr,* 159 U. S. 78, 82, 83, 40 L. ed. 82-84, 15 Sup. Ct. Rep. 1002.

"If the absence of such determining declaration leaves to the statute a double sense, it is the command of the cases that that which rejects retroactive operation must be selected.

"The circumstances of this case impel to such selection. If retroactivity be accepted, what shall mark its limit? The Circuit Court of Appeals found the interrogation not troublesome. It said: 'Congress would, we think, scarcely be impressed with a practical likelihood that a transfer made many years before a grantor's death (say twenty-five years, to use plaintiff's suggestion) would be judicially found to be made in contemplation of death under the legal definition applicable thereto, and without the aid of the two years' prima facie provision.' In other words, the sense of courts and juries, good or otherwise, might, against the words of the statute, and against what might be the evidence in the case, unhelped by the presumption declared, fix the years of its retrospect. This would seem to make the difficulty or ease of proof a substitute for the condition which the statute makes necessary to the imposition of the tax; that is, the disposition with which the transfer is made; and certainly whether that disposition exist at an instant before death or years before death, it is a condition to the tax.

"The construction of the Government is more tenable though more unrestrained. It accepted in bold consistency, at the oral argument, the challenge of twenty-five years, and a ruling of the Commissioner of Internal Revenue, in bolder confidence, extends the statute to 'transfers of any kind made in contemplation of death *at any time whatsoever* (italics ours) prior to September 8, 1916.' The sole test in the opinion of that officer is 'the date of the death of the decedent.' He prefixes no period to the retrospect he declares, but reserves, if he be taken at his word, the transfers of all times to the demands of revenue. In this there is much to allure an administra-

tive officer. Indeed, its simplicity attracts anyone. It removes puzzle from construction and perplexity and pertinence on account of the distance of death from the transfer, risking no chances of courts or juries, in repugnance or revolt, taking liberties with the Act to relieve from its exactions to satisfy the demands of revenue.

"If Congress, however, had the purpose assigned by the Commissioner, it should have declared it; when it had that purpose it did declare it. In the Revenue Act of 1918 (February 24, 1919, 40 Stat. at L. 1097, chap. 18, Comp. Stat. Sec. 6336 3-4c) it re-enacted Sec. 202 of the Act of September 8, 1916, and provided that the transfer or trust should be taxed whether 'made or created before or after the passage' of the Act. And we cannot accept the explanation that this was an elucidation of the Act of 1916, and not an addition to it, as averred by defendant, but regard the Act of 1918 rather as a declaration of a new purpose; not the explanation of an old one. But granting the contention of the defendant has plausibility, it is to be remembered that we are dealing with a tax measure, and whatever doubts exist must be resolved against it."

In the even more recent case of *U. S. v. Merriam*, 263 U. S. 179, this court took the same view. Holding that a bequest in a will, in lieu of compensation as executor thereof, did not render the bequest subject to income tax under the Act of 1917, the court said:

"On behalf of the Government it is urged that taxation is a practical matter, and concerns itself with the substance of the thing upon which the tax is imposed, rather than with legal forms or expressions. But in statutes levying taxes the literal meaning of the words employed is most important, for such statutes are not to be extended by implication beyond the clear import of the language used. If the

words are doubtful, the doubt must be resolved against the Government and in favor of the taxpayer. *Gould v. Gould,* 245 U. S. 151, 153, 62 L. ed. 211, 213 38 Sup. Ct. Rep. 53."

So also in *U. S. v. Whitridge,* 231 U. S. 144, 58 L. Ed. 159, it was held that the income derived from the management of street railway lines by receivers authorized and required by the order for their appointment to manage and operate such railways is not subject to the excise tax imposed by the Act of August 5, 1909, upon the doing or carrying on of business in a corporate capacity. In announcing the court's decision, Mr. Justice Pitney said:

"A reference to the language of the Act is sufficient to show that it does not in terms impose a tax upon corporate property or franchises as such, nor upon the income arising from the conduct of business unless it be carried on by the corporation. Nor does it in terms impose any duty upon the receivers of corporations or of corporate property, with respect to paying taxes upon the income arising from their management of the corporate assets, or with respect to making any return of such income.

"And we are unable to perceive that such receivers are within the spirit and purpose of the Act, any more than they are within its letter. True, they may hold, for the time, all the franchises and property of the corporation, excepting its primary franchise of corporate existence. In the present cases, the receivers were authorized and required to manage and operate the railroads and to discharge the public obligations of the corporations in this behalf. But they did this as officers of the court, and subject to the orders of the court; not as officers of the respective corporations, nor with the advantages that inhere in corporate organizations as such. The

possession and control of the receivers constituted, on the contrary, an ouster of corporate management and control, with the accompanying advantages and privileges."

One of the conspicuous decisions of this court is *Eidman v. Martinez,* 184 U. S. 578. The decision was that American securities passing partly under a will executed abroad by a non-resident alien, and partly under the intestate laws of Spain, are not subject to the inheritance tax imposed by the War Revenue Act of June 13, 1898, Sec. 29, upon personal property passing "either by will or by the intestate laws of any state or territory," since the words "passing by will" are limited by the subsequent words "or by the intestate laws of any state or territory." In reaching this conclusion the court stated the whole rule on the subject, both as to exceptions limiting the taxing power, and as to exemptions open to the taxpayer, as follows;

> "It is an old and familiar rule of the English courts, applicable to all forms of taxation, and particularly special taxes, that the sovereign is bound to express its intention to tax in clear and unambiguous language, and that a liberal construction be given to words of *exception* confining the operation of duty (*Warrington v. Furbor,* 8 East, 242, 247; *Williams v. Sanger,* 10 East, 66, 69; *Denn ex dem. Manifold v. Diamond,* 4 Barn. & C. 243, 245; *Tomkins v. Ashby,* 6 Barn. & C. 541; *Doe ex dem. Scruton v. Smith,* 8 Bing. 146, 152; *Wroughton v. Turtle,* 11 Mees. & W. 561, 567; *Gurr v. Scudds,* 11 Exch. 190), though the rule regarding *exemptions* from general laws im-

posing taxes may be different. *Cooley, Taxn.* 146; *Re Enston,* 113 N. Y. 174, 177; *sub. nom. People v. Sherwood,* 3 L. R. A. 464, 21 N. E. 87."

In the controversy recently pending in this court regarding the validity of the tax on gifts imposed by the act of June 2, 1924, this court, in *Blodgett v. Holden,* 275 U. S. 142, held that it would not so construe the statute, in the absence of clear language requiring such construction, so as to apply to a gift made prior to the passage of the Act, and prior to its introduction and consideration in Congress.

In *Untermyer v. Anderson,* 276 U. S. 440, the court held that although the bill was pending and under consideration in Congress at the time the gifts in this case were made, yet it was not applicable, because its provisions, as applied to such gifts, were arbitrary and invalid under the due process clause of the Fifth Amendment; and in *Bromley v. McCaughn,* 280 U. S. 124, the court held the Act valid as to gifts made subsequent to its passage. All of these decisions were by a divided court.

CONCLUSION

For the reasons, therefore:

1. That this corporation never was subject to the tax now sought to be recovered;

2. Even if the corporation was subject to the tax, the stockholders who received their distribution before the passage of the law, are not liable for it, the Government being in the position of a subsequent creditor as to them;

3. Even if the corporation were originally liable, yet it made its return, as provided by statute, and is entitled to the protection of the limitations contained in the Acts of 1921, 1924 and 1926;

4. Even if no return was made, yet the corporation is entitled to the protection of Section 278 (d) of the Act of 1926, because the suit was brought more than six years after the assessment;

5. And, finally, there is no "trust fund" theory which will aid the Government in overcoming these objections to the suit;

It is respectfully submitted that the decisions of the district court and circuit court of appeals should be affirmed.

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Attorneys for Respondents.

APPENDIX

Section 13 (b) Revenue Act of 1916 (39 Stat. 771):

"(b). Every corporation, joint-stock company or association, or insurance company, subject to the tax herein imposed, shall, on or before the first day of March, nineteen hundred and seventeen, and the first day of March in each year thereafter, or, if it has designated a fiscal year for the computation of its tax, then within sixty days after the close of such fiscal year ending prior to December thirty-first, nineteen hundred and sixteen, and the close of each such fiscal year thereafter, render a true and accurate return of its annual net income in the manner and form to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and containing such facts, data, and information as are appropriate and in the opinion of the commissioner necessary to determine the correctness of the net income returned and to carry out the provisions of this title. The return shall be sworn to by the president, vice-president, or other principal officer, and by the treasurer or assistant treasurer. The return shall be made to the collector of the district in which is located the principal office of the corporation, company, or association, where are kept its books of account and other data from which the return is prepared, or in the case of a foreign corporation, company, or association, to the collector of the district in which is located its principal place of business in the United States, or if it have no principal place of business, office, or agency in the United States, then to the collector of internal revenue at Baltimore, Maryland. All such returns shall as received be transmitted forthwith by the collector to the Commissioner of Internal Revenue."

Revenue Act of Oct. 3rd, 1917 (40 Stat. 338):

TITLE XIII—GENERAL PROVISIONS.

Sec. 1302. That unless otherwise herein specially provided, this Act shall take effect on the day following its passage.

Section 200, page 302. The term 'taxable year' means the twelve months ending December thirty-first, excepting in the case of a corporation or partnership which has fixed its own fiscal year, in which case it means such fiscal year. The first taxable year shall be the year ending December thirty-first, nineteen hundred and seventeen, except that in the case of a corporation or partnership which has fixed its own fiscal year, it shall be the fiscal year ending during the calendar year nineteen hundred and seventeen.

Page 307, Sec. 212. That all administrative, special, and general provisions of law, including the laws in relation to the assessment, remission, collection, and refund of internal-revenue taxes not heretofore specifically repealed, and not inconsistent with the provisions of this title, are hereby extended and made applicable to all the provisions of this title and to the tax herein imposed, and all provisions of Title I of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, relating to returns and payment of the tax therein imposed, including penalties, are hereby made applicable to the tax imposed by this title.

Reg. 33, Art. 61. A corporation which was dissolved in 1917, prior to passage of war revenue Act of October 3, 1917, is subject to tax under the Act of September 8, 1916, as amended, and also to the war income tax and the war excess profits tax imposed by the Act of October 3, 1917. (*Brady, et al v. Anderson*, 240 Fed. 665) Corporations so situated will make a return on revised Form 1031, covering the

period in 1917 during which it was in business prior to its dissolution. If it shall have previously made a return covering this period and shall have paid any excess profits tax under the Act of March 5, 1917, it shall be entitled to credit for the amount of such tax so paid against any excess profits tax assessable against it under Title II of the Act of October 3, 1917.

Compiled Statutes of Nebraska, 1922.

Section 453. Dissolved corporation may be sued. Any such dissolved corporation may be sued at law or in equity, in and by its corporate name, for or upon any cause of action accrued, or which but for such dissolution would have accrued against such corporation, in the same manner and with the like effect as if such corporation were not dissolved, and all process by which any suit, either at law or in equity, may be instituted against any such dissolved corporation, may be served by the sheriff or any other proper officer by delivering to any one of the assignees, trustees, receivers or persons having charge of the assets of such dissolved corporation a copy thereof, or by leaving such copy at the residence of any such assignee, trustee, receiver or person having charge of such assets.

Section 468. Dissolution. No corporation can be dissolved by the members thereof, except by consent of two-thirds of all its members, which consent must be entered on its records, unless a different rule has been adopted in its articles of incorporation.

Section 700. Report of dissolution-occupation tax. Each domestic corporation in case of dissolution or revocation of its charter shall file with the secretary of state a certificate of such dissolution or revocation of its charter; in case of dissolution by voluntary action of the corporation, such certificate shall be signed by the president and secretary of the corporation. * * *.

Section 447. Upon its dissolution, by the expiration of the terms of its charter, or otherwise, of any corporation now existing, or hereafter created, and unless other persons be appointed by the legislature or by some court of competent authority, the directors or managers of the affairs of such corporation, acting last before the time of its dissolution, by whatever name they may be known in law, and the survivors of them, shall be the trustees of the creditors and stockholders of the corporation dissolved, and shall have full power to settle the affairs of the same, collect and pay the outstanding debts and divide among the stockholders the money and property that shall remain, in proportion to the stock of each stockholder paid up, after the payment of debts and necessary expenses * * *.

Regulation 33, Article 196, effective January 6th, 1914 to December 31st, 1921, was as follows:

"Where the required returns are not filed within the prescribed time, either by individuals or corporations, notice on Form 1045 should in each case be sent to the delinquent."

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CHARLES ELMORE C
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In the Supreme Court of the United States

No. 340

OCTOBER TERM, 1929

UNITED STATES OF AMERICA,
Petitioner,

vs.

NELSON B. UPDIKE, et al.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR GEORGE A. ROBERTS, RESPONDENT

WARREN H. HOWARD,
FRANCIS A. BROGAN,
ALFRED G. ELLICK,
Attorneys for Respondent.

COCKLE PRINTING CO., LAW BRIEFS, OMAHA

INDEX

	Page
Nature of the Suit	1
Questions Presented	2
Statement of Facts	4
Argument	8
I. The Collection of the Sum Sought to be Recovered Herein from the Defendants as Transferees of the Assets of the Updike Grain Company is Barred by Section 278 (d) of the Revenue Act of 1926	8
1. Is this a proceeding to collect a tax?	9
Government Pleadings	10
Intention of Congress	13
Construction by General Counsel of Bureau of Internal Revenue	18
Construction by the Courts	20
Construction by Department of Justice and Attorneys for Bureau of Internal Revenue	23
Construction by Commissioner of Internal Revenue	25
Construction by Board of Tax Appeals	26
2. Is Section 278 (d) of the Revenue Act of 1926 inapplicable if it should be determined that the taxpayer filed no return	30
History of Section 278 (a)	31
II. The Collection of the Sum Sought to be Recovered Herein from the Defendants, As Transferees of the Assets of the Updike Grain Company, Is Barred by Section 250 (d) of the Revenue Act of 1921 and Section 277 of the Revenue Act of 1924	44
III. If the Collection of These Taxes from the Updike Grain Company, at the Time These Proceedings were Begun, Is Barred by the Limitations Contained in any of the Revenue Acts, this Suit Cannot be Maintained against the Transferees as an Independent Suit for the Recovery of Trust Funds	54
IV. The Assets of the Updike Grain Company were Transferred to the Respondents Herein in August, 1917; The Liability for the Tax Did Not Arise in any event until the Passage of the Revenue Act of 1917, on October 3, 1917, and This Suit Against Such Transferees Cannot Be Maintained, Because the Government Thereby If At All, Became a Creditor for such Tax Subsequent to the Time the Transferees Received the Assets, There Being at the Time of Transfer No Tax Liability Nor an Existing Statute Under Which a Tax Liability Could Arise	56

Page

V. The Provisions of the Revenue Act of October 3, 1917, Are Not Applicable to a Corporation which was Lawfully Dissolved under State Law, after having Discharged all its Existing Obligations and Distributed all its Assets among its Stockholders, Prior to the Enactment of the Suit 59

TABLE OF CASES

Page

Anderson vs. Railway Co., 216 Fed. 83 61
Angier Corp. v. Commissioner, 17 B. T. A. 1376 27
Atkins vs. Bender, 26 Fed. (2d) 690 37

Bank vs. Braithwaite, 7 N. D. 352, 75 N. W. 244 55
Barron-Anderson Co. vs. Commissioner, 17 BTA 686 27
Board of Commissioners v. Tome, 153 Fed. 81 56
Bowers, etc. vs. New York & Albany Lighterage Co., 273 U. S. 346, 47 S. Ct. Rep. 389, 71 L. Ed. 676 9
Brady, et al. v. Anderson, 240 Fed. 665 46
Brewster vs. Gage, ... U. S. 29
Buttolph vs. Commissioner, 29 Fed. (2d) 695 30

Coleman vs. Hagey, 252 Mo. 102 54

Dole vs. Wilson, 39 Minn. 330, 40 N. W. 161 55

Felland vs. Wilkinson, 33 Fed. (2d) 961 22-23
Fisher vs. Woodard, 103 Neb. 253 55
Flagg vs. Flagg, 39 Nebr. 229 55
Florsheim Dry Goods Co. vs. U. S., ... U. S. 44
Fogg vs. Blair, 133 U. S. 534 54

General Electric Co. vs. Hurd, 171 Fed. 984 56
Gleichman vs. Commissioner, 17 B. T. A. 147 27-28
Gould vs. Gould, 245 U. S. 151 60
Graham vs. LaCrosse, etc. R. Co., 102 U. S. 148, 26 L. Ed. 106 54-56-58

Hilder vs. Commissioner, 17 B. T. A. 1189 27-28
Hollins vs. Brierfield Coal & L. Co., 150 U. S. 371 54-57-58
Holmes vs. Webster, 98 Nebr. 105 55
Hospes vs. Northwestern Mfg. Co., 48 Minn. 174 54-58
Hynes vs. Commissioner, 16 B. T. A. 1272 27

Leudecke vs. Des Moines Cabinet Co., 140 Ia. 223 54
Lucas vs. American Code Co., ... U. S. 30

McAleer vs. Clay County, 42 Fed. 665 55-56
McDonald vs. Williams, 174 U. S. 397 54
Mattingly vs. Nye, 8 Wall. 370 58
Merchants Nat. Bk. vs. McDonald, 63 Nebr. 363 55
Mid-Continent vs. Alexander, 35 Fed. (2d) 43 24

TABLE OF CASES (Continued)

	Page
Mullen vs. Hewitt, 103 Mo. 639	56
Nauts vs. Clymer, 36 Fed. (2d) 207	21
Newell vs. Dart, 28 Minn. 243	55
Owensboro vs. Lucas, 18 Fed. (2d) 798	23
Pennsylvania Steel Co. vs. Ry. Co., 198 Fed. 774	61
Pierce vs. U. S., 255 U. S. 398	54-55-57
Ralston vs. Heiner, 24 Fed. (2d) 416	22-23
Ritter vs. U. S., 28 Fed. (2d) 265	51
Robertson vs. Perkins, 129 U. S. 333	58
Routzahn vs. Tyroler, 36 Fed. (2d) 208	24
Russell vs. U. S., 278 U. S. 181	20-21-33
Schwab vs. Doyle, 258 U. S. 529	60
Scott vs. Neely, 140 U. S. 106	55
Scott vs. Western Pac. R. Co., 246 Fed. 545	61
Sexton vs. Wheaton, 8 Wheaton 229	58
Shaw vs. Robinson & Stokes, 50 Neb. 403	54-58
Smietanka vs. First Tr. & Sav. Bk., 257 U. S. 602	60
Southwestern Investment Co. vs. Commissioner, ... B. T. A.	27-28
Spencer vs. Commissioner, 11 B. T. A. 437	26-27-28
State Bank vs. Morse, 60 Kas. 526	58
Trinacia vs. Clarke, 34 Fed. (2d) 325	24-25
Tucker vs. Alexander, 275 U. S. 228	51
Union Trust Co. vs. McCaughan, 24 Fed. (2d) 459	51
Union Trust Co. vs. Wardell, 258 U. S. 537	60
U. S. vs. Armstrong, 26 Fed. (2d) 227	21
U. S. vs. Cabots, 5 Fed. Tax Rep. 6172	21
U. S. vs. Carver, 260 U. S. 482	59
U. S. vs. Jackson, ... U. S.	29
U. S. vs. Kemp, 12 Fed. (2d) 7	23
U. S. vs. Lazenby, 5 Fed. (2d) 827	20-21
U. S. vs. Minnesota, 270 U. S. 181	30
U. S. vs. Snook, 24 Fed. (2d) 844	21-22
U. S. vs. Updike, 25 Fed. (2d) 746 (D. C.)	43
U. S. vs. Updike, 32 Fed. (2d) 1 (C. C. A.)	34
U. S. vs. Whyel, 19 Fed. (2d) 260	21
Updike, et al vs. U. S., 8 Fed. (2d) 913 (C. C. A.)	59
Wheeler vs. Commissioner, 16 B. T. A. 96	27-28
Zeller vs. U. S., 35 Fed. (2d) 870	51

GENERAL COUNSEL'S MEMORANDA

	Page
G. C. M. 1029 VI-2, 115	19, 27, 28
2408 VI-2, 95	19
2408 VI-41, 3461	37
2513 VI-45, 3496	37
2939 VI-1, 144	35
2939 VI-6, 3597	37
4554 VI-2, 86	20

REVENUE LAWS

Revenue Act of 1916:		
Sec. 13 (b)	(39 Stat. 771)	4, 45
14 (a)	(39 Stat. 772)	31, 46, 52
14 (b)	(39 Stat. 772)	52
Revenue Act of October 3, 1917:		
Sec. 4	(40 Stat. 302)	46
200	(40 Stat. 302)	45
212	(40 Stat. 307)	45, 46
Revenue Act of 1921:		
Sec. 250 (d)	(42 Stat. 265)	2, 31, 32, 44
Revenue Act of 1924:		
Sec. 277 (a) (2)	(43 Stat. 299)	2, 44, 45
278 (a)	(43 Stat. 299)	32, 33, 51
278 (d)	(43 Stat. 300)	35, 36
1009 (b)	(43 Stat. 341)	35, 36
1009 (c)	(43 Stat. 341)	36
Revenue Act of 1926:		
Sec. 274	(44 Stat. 55)	16
277	(44 Stat. 58)	33
278 (a)	(44 Stat. 59)	31, 32, 33, 51
278 (c)	(44 Stat. 59)	20
278 (d)	(44 Stat. 59)	2, 8, 16, 17, 30, 35, 54, 55, 58
280 (a) (1), (b) (1) (2)	(44 Stat. 61)	13, 14, 18, 19
1109 (b), (a) (1) (2) (3)	(44 Stat. 114)	34, 35, 53, 54
Sec. 3176, R. S. U. S., as amended by Sec. 16, Rev. Act. 1916		46
Sec. 3224, R. S. U. S.		22, 23, 24
Revenue Act of 1928:		
Sec. 311	(45 Stat. 860)	29, 34
Sec. 604	(45 Stat. 873)	24
Sec. 607	(45 Stat. 874)	20

REGULATIONS BUREAU OF INTERNAL REVENUE

	Page
Reg. 33, Art. 177	53
33, Art. 184	53
33, Art. 186	50
33, Art. 196	4
33, Art. 221	50
33, (Rev.) Art. 42	53
33, (Rev.) Art. 61	46, 47
45, Art. 1012	50

MISCELLANEOUS CITATIONS

	Page
Conference Report to the House, pp. 43, 44, on Rev. Bill of 1926	14, 15
Conference Report to the House, on Rev. Act of 1926, dated Feb. 22, 1926, pp. 39, 42, 43, 44	16, 42, 43
Report of Joint Committee on Internal Revenue Taxation, on Sec. 280, Vol. I, pp. 15, 67	15, 16
Report of Committee on Finance of Senate, upon Rev. Act of 1924, pp. 39, 40, 41, 49, 50, 51, 52	38, 39, 40, 41, 42
Report of Committee on Finance of Senate, dated Jan. 16, 1926, pp. 28, 29, 30	16
Report of Committee on Ways and Means of the House, p. 10, on Rev. Act of 1926, dated Dec. 7, 1925	16, 42

APPENDIX

		Page
Revenue Act of 1916:		
Section 13 (b),	(39 Stat. 771)	63
Revenue Act of 1917:		
Section 4,	(40 Stat. 302)	64
Section 200,	(40 Stat. 302)	64-5
Section 212,	(40 Stat. 307)	65
Section 1004,	(40 Stat. 325)	65-6
Revenue Act of 1924:		
Section 278 (a) (d) (e)	(43 Stat. 299)	66
Revenue Act of 1926:		
Section 277 (a) (1) (2) (3) (4)	(44 Stat. 58)	67-8
Section 278 (a) (d) (e)	(44 Stat. 59)	68
Section 280 (a) (1) (b) (1) (2)	(44 Stat. 61)	69
Section 311 (a)	(44 Stat. 77)	69
Section 1109 (a) (2)	(44 Stat. 114)	70
REGULATIONS:		
Regulation 33, Article 21		70
Regulation 33, Article 186		70-1
Regulation 33, Article 196		71
Regulation 33, Article 197		71
Regulation 33 (Rev.), Article 214, Para. 629		71
Regulation 33 (Rev.), Article 221, Para. 639		72
Regulation 45, Article 1012		72
When issued		73

In the
Supreme Court of the United States

No. 340

OCTOBER TERM, 1929

UNITED STATES OF AMERICA,
Petitioner,

vs.

NELSON B. UPDIKE, et al.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR GEORGE A. ROBERTS, RESPONDENT

NATURE OF THE SUIT

This is a proceeding begun April 2, 1927, to collect a tax from the former stockholders of the Updike Grain Company, dissolved in August, 1917, as transferees of the assets of that company, which tax was assessed against that company in January, 1920, under the Revenue Act of October 3rd, 1917, upon the income of that company, for the fiscal period January 1, 1917, to June 30, 1917.

QUESTIONS PRESENTED

I.

The collection of the sum sought to be recovered herein from the defendants, as transferees of the assets of the Updike Grain Company, is barred by Section 278 (d) of the Revenue Act of 1926. (44 Stat. 59).

II.

The collection of the sum sought to be recovered herein from the defendants, as transferees of the assets of the Updike Grain Company, is barred by Section 250 (d) of the Revenue Act of 1921 (42 Stat. 265) and Section 277 of the Revenue Act of 1924. (43 Stat. 299).

III.

If the collection of these taxes from the Updike Grain Company, at the time these proceedings were begun, is barred by the limitations contained in any of the revenue acts, this suit cannot be maintained against the transferees as an independent suit for the recovery of trust funds.

IV.

The assets of the Updike Grain Company were transferred to the respondents herein in August, 1917, the liability for the tax did not arise in any event until the passage of the Revenue Act of 1917, on October 3rd, 1917, (40 Stat. 300-338), and this suit against such transferees cannot be maintained, because the Government thereby, if

at all, became a creditor for such tax subsequent to the time the transferees received the assets, there being at the time of transfer no tax liability nor an existing statute under which a tax liability could arise.

V.

The provisions of the Revenue Act of October 3, 1917, are not applicable to a corporation which was lawfully dissolved under state law, after having discharged all its existing obligations and distributed all its assets among its stockholders, prior to the enactment of said act.

STATEMENT OF FACTS

While the statement contained in the Government's brief is only inaccurate, in that it is stated on page 4 that no returns were ever filed in behalf of the corporation under the Revenue Act of 1917, and on page 5 that the present suit was begun under the "trust fund" doctrine to recover "funds" received by the stockholders to the use of the United States, yet it omits portions of the record necessary to a full understanding of the issues presented by the respondents herein.

The Updike Grain Company was a corporation organized under the laws of the State of Nebraska, and was dissolved pursuant to those laws during the month of August, 1917. Prior to its dissolution it had paid all its debts and obligations of every character, including all taxes which had accrued, or could accrue, to the Government of the United States under the then existing revenue laws (R. 91, 127).

Under the revenue laws, the Updike Grain Company had selected a fiscal year as the basis of its federal taxation, which terminated on June 30, 1917 (R. 161). Within sixty days thereafter it filed an income tax return on Form 1031 (Revised October 1916) and a profits tax return on Form 1095, pursuant to the provisions of Sec. 13 (b) of the Revenue Act of 1916, (39 Stat. 771) fully set forth in the appendix to this brief. The income shown in those returns is the sole basis of the claim of the Government for the taxes accruing under the Act of October 3, 1917. Although the corporation remained in existence after June 30, 1917, until its dissolution in Au-

gust of that year, yet it is not claimed by the Government that it transacted any business, nor is any claim made for taxes accruing after that period. Not only did the taxpayer report fully and honestly to the Government, all income received by it, and every fact, regarding the income, called for by existing laws and treasury regulations, (R. 107) but, by an unintentional error in calculation, it reported a greater income than it was actually taxable for, and the effect of the Government's audit was to reduce the taxable income of the taxpayer for that period (R. 113, 145).

It is true that Form 1031 (revised January, 1918) was mailed to the taxpayer, in the usual course of mailing blank returns to all taxpayers and was received by its former secretary, in March, 1918, seven months after its dissolution, but he immediately returned it with a letter stating that the corporation was dissolved, that it had filed its returns showing all the income which it had received up to the time of its dissolution, had paid all taxes accruing to the United States Government under existing laws and regulations, and also called attention to the fact that subsequent to its dissolution it had made final returns, showing all its income (R. 91). Thereafter no action was taken by the Bureau of Internal Revenue under Regulation 33, Article 196, in effect from January 6, 1914, to December 31, 1921, (see appendix), by sending to the taxpayer a notice on Form 1045, or by making other demand for returns (R. 349).

During the month of October, 1918, an agent of the Internal Revenue Bureau examined the books and records of the Updike Grain Company for the fiscal years end-

ing in 1913, 1914, 1915, 1916, and 1917, to determine its tax liability for said years, and the fiscal period in 1917 ending June 30, 1917 (R. 95). When he called at the former office of the company and conferred with its former secretary he asked for copies of the returns which the company had made for the fiscal year ending June 30, 1917, and these were furnished and used by him in making his audit (R. 350). The agent made up returns upon the forms then in effect, a corporation income tax return on Form 1031, revised January, 1918, and a corporation excess profits tax return on Form 1103 (R. 131-35). These returns were not signed, but it is significant that the agent of the Bureau, in preparing and transmitting them, (to the commissioner), denominated them "amended returns." In his report to the Department (R. 107) the agent sent in the draft of amended returns, unsigned. When this report was transmitted by the Omaha office to the Commissioner's office in Washington, it was accompanied by a letter (R. 105) in which the agent's action is referred to as a report "of the returns of annual net income of the Updike Grain Company." In subsequent correspondence between the Omaha office and the Washington office on the subject (R. 101) this report of the Revenue Agent is referred to as "supplemental return, fiscal year ended June 30, 1917." In a letter from the Revenue Agent in Charge at Omaha to the Updike Grain Company (R. 317) and another letter of November 24th, 1919 (R. 323), and in various copies, reports, official actions and records, the returns made by the Updike Grain Company, within sixty days from the close of its fiscal year ending June 30, 1917, were referred to as the returns of the corporation for the taxable period then

under consideration, and in all the transactions of the Government officials concerning them they are treated and referred to as amendments, supplements or revisions of those returns and were recognized, accepted and adopted as returns under the Revenue Act of October 3, 1917. In January, 1920, the Commissioner of Internal Revenue assessed a tax against the Updike Grain Company for the amount now sought to be collected in this suit, and, among other entries in the Government records, stamped upon the income tax return of the company made by it in July, 1917, for the fiscal period in question, the assessment in the amount sought to be recovered herein (R. 165).

The defenses presented in the lower court were that no tax ever accrued against the Updike Grain Company, that the stockholders were not liable for the subsequent obligations of the company, if any existed, and that the suit was barred by the limitation provisions of the revenue laws of 1921, 1924 and 1926.

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ARGUMENT

I.

The Collection of the Sum Sought to be Recovered Herein from the Defendants as Transferees of the Assets of the Updike Grain Company is Barred by Section 278 (d) of the Revenue Act of 1926.

The full text of Section 278 (d) of the Revenue Act of 1926 appears in the appendix, but the applicable part to this case is, as follows:

> "Where the assessment of income, excess profits, or war profits tax imposed * * * by prior act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax."

The following concessions are made by the Government in its brief or are undisputed in the record:

(a) That the amount sought to be recovered herein represents income, excess profits and war profits taxes imposed by a prior Act of Congress, to-wit: The Revenue Act of 1917. (Gov. Brief, 4).

(b) That the taxes were assessed against the taxpayer before the enactment of the Revenue Act of 1926. (Gov. Brief, 4).

(c) That the taxes were assessed in January, 1920. (Gov. Brief, 4).

(d) That this suit was begun April 2, 1927, more than six years after the assessment of the taxes was made. (Gov. Brief, 5).

(e) That no other suit or proceedings has been begun against the taxpayer, the stockholders, these respondents, or any one else, for collection of the taxes. (Gov. Brief, 5).

(f) There were no waivers or consents by the taxpayer or any one else, extending the time for assessment or collection of the taxes.

The Government in its brief contends that Section 278 (d) does not bar this suit, (1) because this is not a proceeding to collect taxes, (2) because the taxpayer filed no return, in which case the tax could have been assessed "at any time," which is not a "statutory period of limitation properly applicable thereto."

We will discuss these contentions in the order enumerated, keeping in mind the rule of construction announced by this court in *Bowers v. New York & Albany Lighterage Co.*, 273 U. S. 346, that limitation provisions in a Revenue Act take on the same rule of construction applicable to other provisions of Revenue laws, to-wit: that same "are to be interpreted liberally in favor of the taxpayer," and doubts are to be resolved against the Government.

1.

Is this a proceeding to collect a tax?

It has been the uniform and continuous understanding of Congress, the General Counsel of the Bureau of

Internal Revenue, this court and other Federal courts, the Department of Justice, the attorneys for the Bureau of Internal Revenue, the Commissioner of Internal Revenue and the Board of Tax Appeals, in decisions expressly acquiesced in by the Commissioner of Internal Revenue, that proceedings against transferees of the assets of a taxpayer to collect a tax assessed against the taxpayer are "proceedings to collect a tax", and the proceedings in this case were so understood and declared to be such in the pleadings filed herein, with the approval of the Commissioner of Internal Revenue, the Department of Justice and the attorneys for the Bureau of Internal Revenue.

GOVERNMENT PLEADINGS

In the letter of C. R. Nash, acting Commissioner of Internal Revenue, to the United States District Attorney at Omaha, dated March 21st, 1927, authorizing the institution of this suit (R. 149), it is stated:

> "Reference is made * * * to the matter of beginning a suit in equity against the former stockholders of the Updike Grain Company, a dissolved corporation, to collect additional income and excess profits taxes assessed against said corporation in the amount of $373,911.54, for the eleven months' period ended June 30, 1917."

In a telegram from Blair, Commissioner, to the United States District Attorney, dated April 2, 1927, the date the suit was instituted (R. 153) the Commissioner expressly approved the bill of complaint as filed and authorized its filing.

The bill of complaint, as filed and subsequently amended, except as otherwise indicated, was against sixty-seven stockholders as defendants (R. 1), thirty-nine of whom were residents of Nebraska (R. 2, 3) and thirty-two of whom were served with writs of subpoena, and are respondents in this proceeding. (R. 81, 397). The allegations were, as follows:

> Paragraph XIX (R. 5): "This is a suit in equity brought by the United States of a civil nature arising under a law of Congress providing for internal revenue and the collection thereof."

On the last day of the trial of the case (R. 64), this paragraph was amended to read, as follows:

> "This is a suit in equity brought by the United States of a civil nature." (R. 12).
>
> Paragraph XXIII (R. 8): "Complainant says that there is due and owing to it, the said complainant, from said Updike Grain Company, on account of the matters and things hereinbefore set forth the sum of $373,911.54, together with interest thereon, as provided by law, from the time said amount became due."
>
> Paragraph XXVI (R. 10): "By reason of the said dissolution and distribution of all the assets, said corporation was left without money, assets or property of any kind with which to pay the said taxes due and owing to the United States, and the defendants received the entire money, assets and property charged with a trust in favor of the United States to the extent of the said taxes due and unpaid by it as hereinbefore set forth."
>
> Paragraph XXVII (R. 10): "That the complainant has no plain, adequate or complete remedy at law against said Updike Grain Company or the defendants."

> Paragraph XXVIII (R. 10): "That the Commissioner of Internal Revenue authorizes and sanctions these proceedings."

This paragraph was also amended at the trial by interlineation by adding after the words "Internal Revenue," the words "and the Attorney General of the United States." (R. 160).

Paragraph XXIX (R. 11) is the prayer, wherein the complainant prayed:

> "That this Court decree that the corporate assets of said Updike Grain Company so distributed to the defendants constitute a trust fund for the payment of said taxes due and owing by the said corporation to the United States, and that the said defendants shall account to this court for the aforesaid trust property, and that the fund aforesaid be applied to the payment of said taxes due and owing to the complainant."

In the opinion of the trial court by Honorable T. C. Munger, D. J., filed April 13th, 1928, it is stated:

> "The purpose of the suit is to recover the amount of the tax assessed against the defendant [Updike Grain Company] from the transferees of the corporate assets." (R. 65).
>
> "But in this case an assessment was made. It was made by the Commissioner of Internal Revenue. It is the foundation of this suit." (R. 67).
>
> "The United States delayed proceedings for the collection of the tax it claims to be due from defendants." (R. 69).

In the opinion of the Circuit Court of Appeals, filed March 21st, 1929, it is said:

> "While this is a case against transferees, we must consider that it is a proceeding in court to collect a tax, notwithstanding that it is an action against transferees." (R. 394).

CONGRESS

Congress has at all times understood and recognized proceedings of this character to be proceedings for the collection of taxes, in the following particulars:

(a). Congress first took cognizance of proceedings against transferees to collect taxes in the Revenue Act of 1926, by the enactment of Section 280 of that Act (44 Stat. 61), wherein it provided for summary proceedings against transferees of property of a taxpayer for the collection of the tax imposed upon the taxpayer, identical with the summary proceedings therein provided against the taxpayer, to-wit: By notice of intention to assess the liability for the tax against the transferee, with an opportunity to appeal to the Board of Tax Appeals within sixty days from the date of the notice, failing in which to be thereafter deprived of the right to question the assessment in court or otherwise. The only justification for such a summary procedure would be that it was for the collection of a tax, otherwise such a procedure would not constitute due process of law.

The provisions of Section 280, indicating that proceedings against transferees were proceedings to collect a tax, and are subject to all of the limitations against the taxpayer, are as follows:

Sec. 280 (a) "The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this title (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

"(1) The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this title or by any prior income, excess-profits, or war-profits tax Act."

(b). In the Conference Report to the House of Representatives on the Revenue Bill of 1926, dated February 22d, 1926, at pages 43 and 44, the purport of Section 280 was stated to be, as follows:

"Without in any way changing the extent of such liability of the transferee under existing law, the amendment enforces such liability (whether in respect of the tax as originally returned by the taxpayer or a deficiency therein) in the same manner as liability for a tax deficiency is enforced; that is, notice by the Commissioner to the transferee and opportunity either to pay and sue for refund or else to proceed before the Board of Tax Appeals, with review by the courts. Such a proceeding is in lieu of the present equity proceeding and is exclusive, save that, of course, in a proper case, a tax lien upon the assets arising prior to their transfer may be enforced against the transferee by distraint, or in case of real estate by a proceeding in equity. In the case where the taxpayer remains in existence after the transfer, an unsatisfied return of a distraint warrant, issued in pursuance of an assessment lawfully

made after a deficiency letter has been mailed to the taxpayer, would suffice in lieu of an unsatisfied execution to establish the liability of the taxpayer.

"In view of the above situation it will be seen that the amendment makes the procedure for the collection of the amount of the liability of transferees conform to the procedure for the collection of taxes. The amendment thereby substitutes the specialized and more expeditious procedure of the board for that of the district courts in equity and will develop through the board a uniformity of precedents in lieu of the present rather vague principles of law governing the liability of a transferee for unpaid taxes of a transferor. * * *

"Under the amendment the liability of the taxpayer for the tax, including all interest and penalties, is fixed as of the time of the transfer of the assets.

* * * * *

"The statute of limitations as to collection is covered by the incorporation by reference of section 278 (d)."

(c) In the report, dated November 15, 1927, of The Joint Committee on Internal Revenue Taxation, established under Section 1203 of the Revenue Act of 1926 (44 Stat. 127), made after it had been uniformly held and ruled by all departments of the Government, that the limitation provisions affecting the collection of taxes against taxpayers, applied to transferees, it was stated on page 67, in referring to the effect of Section 280, as follows:

"In substance it subjects him to the same proceeding, as though he were the taxpayer."

and on page 68:

"At present no change is recommended as to limitation proceedings."

(d) Congress sought in Section 280 to make the summary proceedings provided in Section 280 the exclusive procedure against transferees. That is not only indicated by the language of Section 280, which required that the liability of transferees should be assessed and collected in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed upon the taxpayer, which was exclusively by the provisions of Section 274 of the Revenue Act of 1926 (44 Stat. 55), but also in the Report of the Committee on Ways and Means to the House, dated December 7, 1925, Page 10, the Report of the Committee on Finance of the Senate, dated January 16, 1926, Pages 28, 29 and 30, the Statement of the Managers on the Part of the House, contained in the Conference Report to the House on the Revenue Act of 1926, dated February 22d, 1926, Pages 39, 43 and 44, and the Report of The Joint Committee on Internal Revenue Taxes, dated November 15th, 1927, Page 15.

No such attempt could be justified unless Congress was acting upon the theory that proceedings against transferees, for the collection of taxes imposed upon a transferor taxpayer, are "proceedings to collect a tax."

The Government in its brief contends that the provisions of Section 280 indicate that Congress did not intend that proceedings against a transferee to collect a tax should be subject to the limitation provisions contained in the Revenue Laws, and bases this contention upon the assertion that by enacting "specific statutes of limitations" in Section 280, Congress indicated an intention to restrict the application of Section 278 (d) in the

same Revenue Act (44 Stat. 59) to proceedings against the taxpayer only.

The Government admits that the terms of Section 278 (d) are broad enough to bar this suit, but seeks to limit its application to proceedings against a taxpayer, only, solely by claiming that Section 280 indicates a contrary intention by Congress, notwithstanding the well settled rule of statutory construction, that in construing plain and unambiguous statutes the intention of congress is not a subject of inquiry.

When we analyze Section 280, however, we find that that section indicates an intention of Congress, entirely consistent with the Reports of its Committees, set forth above, and the contention of respondent.

Bearing in mind that this is a proceeding to "collect" and not to "assess," and that Section 278 (d) deals solely with the right to "collect," it is, therefore, necessary for us to ascertain (1) if Congress did in fact restrict the effect of Section 278 (d) by any "specific statutes of limitation" in Section 280 on the collection of taxes from transferees, and (2) the real intention of Congress in that respect, if possible.

Section 280 deals with limitations upon both the right to *"collect"* a tax from, and the right to *"assess"* a tax against, a transferee, but it deals with the right to *"collect,"* only in the general terms of Paragraph (a) thereof, wherein the general limitation statutes of the Revenue Acts are expressly made applicable to proceed-

ings thereunder against transferees, by the use of the following language:

> "The amounts * * * shall except as hereinafter in this Section provided, be assessed, *collected,* and paid in the same manner and subject to the same provisions and *limitations* as in the case of a deficiency in a tax imposed by this title (* * * including * * the provisions authorizing distraint and proceedings in court *for collection*). (Our italics).

Note the phrase "except as hereinafter in this Section provided." Thereinafter there was no provision otherwise limiting the time *"for collection,"* but there were specific provisions changing the time for *"assessment,"* which simply extended "the period of limitation for *assessment* of any such liability" to "within one year after the expiration of the period for *assessment* against the taxpayer," or if an assessment had been made against the taxpayer before the time for assessing him had expired, to any time within six years after the assessment, but in no case later than one year after the enactment of the 1926 Act, to-wit: February 26, 1926 (Sec. 280 (b) (1) (2), Rev. Act of 1926. (See Appendix).

It must be quite clear from an analysis of Section 280 that Congress expressly made proceedings thereunder, both to assess and collect, subject to limitation statutes contained in other sections of the Act and particularly in Section 278 (d), with the one year extension for assessing, only.

GENERAL COUNSEL BUREAU OF INTERNAL REVENUE

The General Counsel of the Bureau of Internal Revenue in memoranda opinions promulgated for the guidance

of collectors, Revenue Agents and other employees of the Treasury Department, in administering the Revenue laws, has recognized that proceedings against transferees for the collection of their liability for taxes of their transferors, are proceedings to collect a tax and are subject to the provisions of the Revenue Laws.

In G. C. M. 1029, Cum. Bull. VI-1, p. 115, promulgated on January 10, 1927, it was held that Section 280 of the Revenue Act of 1926 had no retroactive application and therefore, if the tax liability of the transferor taxpayer was barred prior to the enactment of the Revenue Act of 1926, the liability of a transferee therefor could not be asserted under Section 280, notwithstanding the one year period after the expiration of the period of limitation for assessment against the taxpayer, as provided in Section 280 (b) (1), had not yet expired; and in that connection the liability of transferees was referred to, as follows:

> "Under that section the transferees' liability is no greater nor more comprehensive than that of the transferor taxpayer. The section merely prescribes a method for the enforcement of an established liability and adopts, for this purpose, the method of assessment applicable to the collection of taxes in the ordinary case. The logical conclusion is that it was not the purpose of Congress to make effective against a transferee a tax liability which at the time of the enactment of the Revenue Act of 1926 could not be asserted against the transferor taxpayer because of the bar of the Statute of Limitations."

In G. C. M. 2408, Cum. Bull. VI-2, p. 95, it was held that a consent in writing signed by a taxpayer, pursuant

to the provisions of Section 278 (c) of the Revenue Act of 1926, (44 Stat. 59), which reads, as follows:

> "Where both the Commissioner and the taxpayer have consented in writing to the assessment of the tax after the time prescribed in Section 277 for its assessment, the tax may be assessed at any time prior to the expiration of the period agreed upon."

extended the time for proceeding against the transferee of the assets of the taxpayer, although Section 278 (c) related only to "the taxpayer."

In G. C. M. 4554, Cum. Bull. VII-2, p. 86, the General Counsel accorded to a transferee the refund rights granted in Section 607 of the Revenue Act of 1928, (45 Stat. 874), where a tax had been paid by a transferee after the expiration of the period of limitation for assessment and collection of the tax against the taxpayer, notwithstanding such rights were granted in that section only to the *"taxpayer"* and related only to *"any tax."*

COURTS

No court has yet held in a suit of this nature that any liability of a transferee existed after the tax liability of the transferor had become barred. On the contrary, the following courts, in addition to the lower courts in this case, have held that when the tax liability of the transferor became barred, the right to proceed against the transferee of the assets of such transferor was likewise barred:

Russell vs. United States, 278 U. S. 181.

United States vs. Lazenby, 5 Fed. (2d) 827, (D. C. N. D. Texas).

United States vs. Whyel, 19 Fed. (2d) 260. (D. C. W. D. Pa.), affirmed 28 Fed. (2d) 30 (3rd C. C. A.)

United States vs. Snook, 24 Fed. (2d) 844 (D. C. N. D. Ga.) Reversed on other grounds 28 Fed. (2nd) 30.

United States vs. Armstrong, 26 Fed. (2d) 227. (8th C. C. A.)

Nauts vs. Clymer, 36 Fed. (2d) 207. (6th C. C. A.).

United States vs. Cabots, 5 Fed. Tax Rep. 6172. (U. S. Ct. Cl.)

In *Russell vs. United States,* supra, being a suit in equity against stockholders of a corporation to collect taxes assessed against the corporation, this court held that the right to collect those taxes from such transferees was barred by the limitation provisions in the Revenue Acts of 1918 and 1921. The Government was conceding that the right to collect the taxes from the transferees was barred, unless the time for collecting same had been extended by Section 278 (d) of the Revenue Act of 1924. This court accepted the view that the proceedings against the transferees were barred, unless the period of limitation had been extended by Section 278, as is evidenced by the following statements in the opinion:

> "Manifestly, but for Section 278, petitioners would be free from liability under the five-year limitation in the Act of 1918, continued by the Act of 1921."

In *United States vs. Lazenby,* supra, the court said:

> "That the instant suit is not against the original taxpayer, but is at equity against a person who re-

ceived all of the assets of the taxpayer, must not prevent a reasonable view of the statute of repose which Congress evidently intended. The language of the statute is that 'no proceeding in court for the collection of such taxes shall be begun after the expiration of such period.' Certainly there can be no other object in the present suit. It is for the collection of a tax."

In *United States v. Snook*, supra, it was said about the suit:

> "Its foundation, to be sure, is a tax claim against the corporation, and in my opinion, if this were barred, this suit would fail."

In the following cases, upon the insistence of the attorneys for the Government, the courts held that Section 3224 of the Revised Statutes providing:

> "That no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court"

applied to suits by transferees to enjoin proceedings to collect their liability for taxes:

Felland vs. Wilkinson, 33 Fed. (2d) 961, (D. C. W. D. Wisc.)

Ralston vs. Heiner, 24 Fed. (2d) 416 (3d CCA)

In *Felland vs. Wilkinson*, supra, the court used this significant language:

> "It must be borne in mind that while the liability of a transferee may not be a tax liability in the ordinary sense, nevertheless it is a liability for a tax; in other words, the government is seeking to collect what is primarily a tax and continues to be

a tax authough, because of the inability to collect from the taxpayer proper, it seeks to require his transferee to pay. From the standpoint of the government the money sought in this case is as much an item of revenue as it would be were the proceedings to collect directed toward the Stoughton Lumber Association."

In *United States vs. Kemp,* 12 Fed. (2d) 7, (5th CCA), being a suit in equity upon the "trust fund" theory against transferees, it was held, upon the insistence of the attorneys for the Government, that a waiver signed by the taxpayer extending the period of time for collection of a tax against the taxpayer, operated to extend the period of time for collection of such tax against the transferees of the taxpayer, thus applying the waiver provisions in Section 250 (d) of the Revenue Act of 1921 (42 Stat. 265) to a transferee, and thereby recognizing the suit to be a proceeding for the collection of a tax.

DEPARTMENT OF JUSTICE AND ATTORNEYS FOR THE BUREAU OF INTERNAL REVENUE

The Department of Justice and attorneys for the Bureau of Internal Revenue have persistently and consistently taken the position in the following court cases, that proceedings against transferees were proceedings to collect taxes and that an attempt by such transferees to enjoin such proceedings came within the inhibitions of Section 3224 of the U. S. Rev. St., quoted supra:

Owensboro Ditcher & Grader Co. vs. Lucas, 18 Fed. (2d) 798, (D. C. W. D. Ky.).

Ralston vs. Heiner, 24 Fed. (2d) 416. (3d CCA).

Felland vs. Wilkinson, 33 Fed. (2d) 961, (D. C. W. D. Wisc.).

Trinacia Real Estate Co. vs. Clark, 34 Fed. (2d) 325, (D. C. N. D. N. Y.)

Mid-Continent Petroleum Corp. vs. Alexander, 35 Fed. (2d) 43, (D. C. W. D. Okla.)

Routzahn vs. Tyroler, 36 Fed. (2d) 208 (6th CCA).

In the case of *Routzahn vs. Tyroler,* the transferee was contending that Section 280 of the Revenue Act of 1926 was unconstitutional, because there was no provision in the Revenue Laws permitting the transferee to appeal to the courts from an adverse ruling by the Board of Tax Appeals, but although the right of review of the decision of the Board of Tax Appeals was given only to a "taxpayer" in the Revenue laws, the Department of Justice and the attorneys for the Bureau of Internal Revenue induced the court to hold that a transferee was a "taxpayer" within the meaning of that "term", as used in Section 1001 of the Revenue Act of 1926 (44 Stat. 109) (Certiorari denied, _____).

It is suggested on p. 14 of the Government's brief, that by the enactment of Section 604 of the Revenue Act of 1928, (45 Stat. 803), prohibiting suits to restrain the enforcement of the liabilities of transferees under Section 280, Congress indicated an intention to treat the liability of transferees as distinct from the liability of taxpayers, because the enactment of that section was not necessary, if Section 3224 R. S. was applicable.

It is quite evident that because of the divergent opinions rendered by the inferior courts, in the cases cited above, with respect to the effect of Section 3224, that Con-

gress simply passed Section 604, undoubtedly at the instance of the Bureau of Internal Revenue, in order to settle this controversy by statute, instead of awaiting an opinion of a court of last resort, and that the inference sought to be drawn by the Government is not justifiable under the circumstances.

COMMISSIONER OF INTERNAL REVENUE

In addition to being a party to the court proceedings and the rulings of the General Counsel, referred to above, the Commissioner of Internal Revenue has upon other occasions taken the position that proceedings against transferees were proceedings to collect a tax.

In the case of *Trinacia Real Estate Co. vs. Clark,* supra, it appears that he made a jeopardy assessment against a transferee under Section 279, Revenue Act of 1926 (44 Stat. 59), which contains no reference to transferees, but only grants the right to the Commissioner to make jeopardy assessments against the "taxpayer." It further appears from the facts in the *Trinacia* case that in the very notices sent out by the Commissioner of Internal Revenue, in proceedings against transferees under Sections 280 and 274, the Commissioner recognizes that such proceedings are for the collection of "a tax", because in the notice sent out in that case, which we assume is the standard form, the Commissioner said:

> "In accordance with the provisions of Section 279 (a) of the Revenue Act of 1926, there has been assessed against you income tax, penalty and interest, amounting to $16,502.66, for the taxable years 1920 to 1926, inclusive, as transferee of the assets of Joseph Falcone * * *. As provided in Section 280 of

the Revenue Act of 1926, there has been assessed against you the amount of $16,502.66 in taxes, penalties and interest, constituting your liability as a transferee of the assets of Joseph Falcone * * * for unpaid income taxes, penalties and interest, in the amount of $16,502.66 assessed against Joseph Falcone * * *."

On December 31st, 1926, the office of the Commissioner of Internal Revenue took the position in the instant case, that the right to proceed against the respondents herein was barred by the limitation provisions in the Revenue Laws, because in a letter of that date, from C. R. Nash, Assistant to the Commissioner, to the Collector of Internal Revenue, at Omaha, Nebraska, (R. 291), it is said:

> "Reference is made to the following tax due from the above named company:
>
> "$373,911.54, assessed on the Commissioner's January 1920 List, Page 14, Line 1.
>
> "This office has decided that there is no liability which can be asserted against Mr. Nelson B. Updike, Omaha, Nebraska, et al, as transferees of the property of the taxpayer, pursuant to the provisions of Section 280 of the Revenue Act of 1926. The amount of tax set forth above should, therefore, be abated as uncollectible on Form 53."

BOARD OF TAX APPEALS

The Board of Tax Appeals has uniformly adhered to the rule that the limitation provisions in the Revenue Laws, respecting proceedings for the collection of a tax are applicable to proceedings against transferees:

> *Spencer vs. Commissioner*, 11 B. T. A. 437, decided April 9, 1928, acquiesced in by Commissioner, July 30, 1928, I. R. B. VII-31-3128.

Wheeler vs. Commissioner, 16 B. T. A. 96, decided April 22, 1929, acquiesced in by the Commissioner, I. R. B. VIII-31-4290.

Hynes vs. Commissioner, 16 B. T. A. 1272, decided June 29, 1929, approved and following the opinion of the CCA in the instant case.

Barron-Anderson Co. vs. Commissioner, 17 B. T. A. 686.

Hilder vs. Commissioner, 17 B. T. A. 1189.

Angier Corporation vs. Commissioner, 17 B. T. A. 1376.

Gleichman vs. Commissioner, 17 B. T. A. 147.

Southwestern Investment Co. vs. Commissioner, _____ B. T. A. _____, decided February 26, 1930.

In the Government's brief, p. 19, it is said that Bureau rulings and Board decisions are not in point, because they were made with reference to proceedings against transferees under Section 280, but in that the Government is in error, because in G. C. M. 1029, supra, and in *Spencer vs. Commissioner*, supra, and *Barron-Anderson Co. vs. Commissioner*, supra, it was held that Section 280 being silent as to whether a transferee may be assessed, where the period of limitation for assessment against the taxpayer expired prior to the enactment of the Revenue Act of 1926 without any assessment or proceedings in court against the taxpayer having been made or begun, they would therefore apply the general rule that the right to enforce a liability against a transferee became barred when the right to enforce the tax against the taxpayer became barred.

We have recently noted that under date of February 4, 1930, the acquiescence of the Commissioner in *Spencer vs. Commissioner,* under date of July 30th, 1928, was revoked, no reason given therefor. This long delayed revocation has all the aspects of a mere gesture for the purpose of this litigation, but G. C. M. 1029 still stands as a ruling for guidance of Revenue agents, attorneys, etc.

In the *Wheeler case,* supra, the Board of Tax Appeals held:

> "Where the liability of the taxpayer is extinguished, by Section 1106 (a) of the Revenue Act of 1926, the liability of a transferee, under Section 280 of the same Act, is also extinguished."

The acquiescence in this decision has not yet been revoked.

The *Gleichman* and *Southwestern Investment Co. cases,* supra, followed the rule in the Wheeler case.

In the *Hilder case,* supra, the Government's attorneys conceded that the right to collect the tax against the transferees was barred, because it was barred against the taxpayer at the time of the enactment of the Revenue Act of 1926, and the Board so held.

The foregoing are decisions by the Board of Tax Appeals, to which Congress has endeavored, in the 1926 and 1928 acts, to give exclusive jurisdiction over proceedings against transferees, and although the Board of Tax Appeals had uniformly been holding contrary to the Government's contention in the instant case, prior to the enactment of the Revenue Act of 1928, Congress did not at-

tempt to disturb those holdings, or the rulings of the Commissioner or the General Counsel of the Bureau of Internal Revenue, or of the courts, as above indicated, by any provision in the Revenue Act of 1928, but re-enacted Sec. 280 in substantially the identical language of the 1926 Act (Sec. 311 Rev. Act of 1928).

In view of the foregoing uniform, consistent and continuous rulings of the Executive Department charged with the administration of the Revenue Laws, and the attitude of congress thereto, the following rules of law announced by this court become pertinent:

In *United States vs. Jackson,* (Dec. 5, 1929), the holding of this court is summarized in the syllabus, as follows:

> "Great weight is properly to be given to the construction consistently given to a statute by the executive department charged with its administration; and such construction is not to be overturned unless clearly wrong, or unless a different construction is plainly required.
>
> "The silence of Congress in the face of a long-continued practice of an executive department involving the construction of a Federal statute must be considered as equivalent to consent to continue the practice."

In *Brewster vs. Gage,* (Jan. 6th, 1930, the holding of this court is summarized in the syllabus, as follows:

> "The practical interpretation of an ambiguous or doubtful statute that has been acted upon by officials charged with its administration will not be disturbed except for weighty reasons.

"The substantial re-enactment in later income tax statutes of a provision theretofore construed by a regulation of the Treasury Department is persuasive evidence of legislative approval of the regulation."

In *Lucas vs. American Code Co.*, (Febr. 24, 1930), the holding of this court is likewise summarized in the syllabus, as follows:

"The interpretation of income tax legislation, and the practice adopted by the department charged with its enforcement should not be interfered with, unless clearly unlawful."

See also

United States vs. Minnesota, 270 U. S. 181.

Buttolph vs. Commissioner, 29 Fed. (2d) 695 (7th CCA).

2.

Is Section 278 (d) of the Revenue Act of 1926 inapplicable if it should be determined that the taxpayer filed no return?

The Government contends that:

(a) The taxpayer filed no return.

(b) The tax could have been assessed or collected by suit, under Section 278 (a) of the Revenue Act of 1926, "at any time."

(c) "At any time" is not a "statutory period" within the meaning of that term as used in Section 278 (d).

In other words, it is claimed that Section 278 (d) does not apply to no-return cases.

We will hereinafter show that returns were filed by the taxpayer in this matter, which set forth all the data necessary to make the assessment, and that those returns were accepted and adopted by the Commissioner as the return of the taxpayer under the October 3, 1917, Act, but for the purposes of this argument we will assume that no returns were filed.

Section 278 (a) of the Revenue Act of 1926 is as follows:

> "In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun *without assessment*, at any time." (our italics).

HISTORY OF SECTION 278 (a)

This section deals with fraudulent return and no-return cases. Prior to the Revenue Act of 1916 there were no limitation provisions in the income tax laws. In the Revenue Act of 1916, among other limitation provisions, was a provision (Section 14 (a)) relieving a taxpayer who failed to file a return, or who even filed an erroneous or fraudulent return, from an assessment or collection of a tax against him, if the Government did not discover that fact within three years after the return was due.

In the Revenue Act of 1918 (Section 250 (d)), a five-year limitation applied to both the assessment and collection of taxes against persons who failed to file a return and the limitation period started to run from the date the return was "due."

In the Revenue Act of 1921, (Section 250 (d)) it was provided:

"That in the case of a false or fraudulent return with intent to evade tax or of a failure to file a required return, the amount of tax due may be determined, assessed and collected and a suit or proceeding for the collection of such amount may be begun at any time after it becomes due."

It will be noted that in the 1921 Act the two separate remedies, of assessing at any time, and of a suit or proceeding for collection at any time, are cumulative, and there is no additional restriction upon the conditions for bringing suit or other proceedings for collection.

Section 278 (a) in the 1924 Act is identical with Section 278 (a) in the 1926 Act and in that Section in the 1924 and 1926 Acts, a marked change was made in the language used in the 1921 Act, by the insertion of the phrase "without assessment" to qualify the clause respecting a proceeding in court to collect. As a result assessments could be made at any time, but a proceeding in court for the collection of the tax could only be begun "at any time" where there had been no assessment. In other words the two remedies of assessment and collection are given in the alternative and a proceeding in court for the collection of a tax was allowed "at any time" only when begun "without assessment."

By permitting a proceeding in court for the collection of the tax, only where no assessment had been made, Congress obviously left open for further treatment a limitation upon proceedings for collection of a tax where an assessment had been made. This limitation appeared in both the 1924 Act and the 1926 Act, in Section 278 (d). In the 1924 Act, Section 278 (d) was limited in subdivi-

sion (e) of that Section, to cases where the assessment had been made after the enactment of that Act (See Appendix) (*Russell vs. United States, supra*).

This Section, in both Acts, permitted proceedings in court for the collection of a tax at any time within six years after the assessment was made, but only, of course, where an assessment had been made within the period of limitation provided in that and other Sections of the Acts. In other respects, this Section in the two Acts was substantially the same, except that the 1924 Act uses the phrase "within the period prescribed in Section 277 or in this Section," whereas, the 1926 Act uses the phrase "within the statutory period of limitation properly applicable thereto." This change of phraseology was adopted throughout the entire 1926 Act, (See Section 278 (d) (e); 311 (b), (c); 1109 (a), (3) and (b) of the 1924 and 1926 Acts), whereas, in the 1924 Act reference was made to specific sections. The obvious purpose of the change was both to obtain uniformity of expression and to avoid an erroneous omission of a section containing a limitation upon an assessment.

With respect to the insertion of the phrase "without assessment" in Section 278 (a) of the 1924 and 1926 Acts, it is important to note that this phrase was also inserted in Section 277 (a), (1), (2), (3) and (4) of the 1926 Act (see appendix), which of course was necessary if there was to be a different limitation period for collection after assessment from the period for assessment.

The Circuit Court of Appeals in its opinion in this case (32 Fed. (2d) 1), stressed the significance of the insertion of this phrase, as follows:

> "Three other amendments were made in 1926, in paragraphs 2, 3, and 4 of the preceding section (277), which are of significance. Prior to the 1926 amendments these paragraphs provided that 'and no proceeding in court for the collection of such taxes shall be begun' after the period fixed in each paragraph for assessment. That is, prior to 1926, the period for assessment or court action were the same; the Government had to assess or sue, or assess and sue, within the particular period, say five years.
>
> "But in 1926 in all three paragraphs the limitation on proceedings in court was qualified by inserting the words 'without assessment,' so that the paragraphs now read 'and no proceeding in court without assessment for the collection of such taxes shall be begun,' etc.
>
> "Take these amendments in connection with 278 (d) quoted above, and the idea of Congress is clear and inescapable. Congress fixed one period (say five years) for the initial move against the taxpayer, whether it be by assessment or suit without assessment, and a different period (6 years) for the second move, distraint or court proceedings, after assessment. For the second move we look to 278 (d) and that alone."
>
> (R. 394, 395).

This phrase "without assessment" was also carried into the limitation provisions affecting estate taxes (Section 311 (a), Revenue Act of 1926) (see appendix), and in what may be termed the general dragnet limitation provisions intended to apply to all revenue taxes, not otherwise specifically provided for. (Section 1109 (a)

(2), Revenue Act 1926) (see appendix). The effect of the insertion of this phrase was recognized in G. C. M. 2939, Cum. Bull. VII-1, p. 144, wherein after setting forth Section 278 (d) and (e) of the Revenue Act of 1924, in discussing the difference in the time limit for "assessment" from the time limit for the "collection" after assessment, Mr. C. M. Charest, General Counsel, says:

> "To the same effect is section 278 (d) and (e) of the Revenue Act of 1926.
>
> "Thus it is apparent that for every case within the purview of the Revenue Act of 1924 a six-year collection period attached after the assessment was made, this regardless of whether the assessment was made before or after the enactment of the Act."

It is quite apparent from the foregoing that Congress intended that after a valid assessment had been made against the taxpayer in any case, whether a return had been filed or not, the time for collecting the tax by proceeding in court was limited to six years from and after such assessment.

It is further contended by the Government that if it should be found in this case that the taxpayer filed no return then under Section 278 (a) the tax could be collected "at any time" and that "at any time" is an unlimited period and therefore cannot be a "statutory period of limitation."

A comparison of Sections 278 (d) and 1109 (b) of the 1924 and 1926 Acts will demonstrate that Congress intended to give to the phrase " within the statutory period of limitation" no such restricted meaning.

In Sec. 278 (d) of the 1924 Act, it is provided:

> "Where the assessment of the tax is made within the period prescribed in Section 277 or in this Section, such tax may be collected by distraint or by a proceeding in court, begun within six years after the assessment of the tax."

When we look for "the period prescribed * * * in this Section," we find that the only "period prescribed" is "at any time."

The word "period" was likewise given the same statutory definition, interpretation or construction in another part of the 1924 Act. In Section 1009 (b) of that Act, it is provided:

> "In case of a false or fraudulent return with intent to evade tax, or a failure to file a required return, or a willful attempt in any manner to defeat or evade tax, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

In Sub-division (c) of the same Section, it is provided:

> "Where the assessment of the tax is made within the period prescribed in subdivisions (a) and (b) such tax may be collected by distraint or by a proceeding in court, begun within six years after the assessment of the tax. Nothing in this Act shall be construed as preventing the beginning, without assessment, of a proceeding in court for the collection of the tax at any time before the expiration of the period provided in subdivision (a) for the beginning of such proceeding."

As there was no other "period prescribed" in Subdivision (b) than "at any time," Congress could only have intended that "period" should mean "at any time."

No such narrow, strained or forced construction or interpretation has been indulged in by the Government when its interests required a contrary construction, because in the following General Counsel's Memoranda and Rulings it has been determined that the phrase "statutory period" as used in Section 278 (d) of the Revenue Act of 1926, means the statutory period plus any additional time extended by waivers, even though the waivers were unlimited as to time.

G. C. M. 2513, Ruling VI-45-3496.

G. C. M. 2939, Ruling VII-6-3597.

G. C. M. 2408, Ruling VI-41-3461.

In *Atkins vs. Bender*, 26 Fed. (2d) 690, (D. C. W. D. La.), the court adopted the same view.

That Congress intended that Section 278 (d) should apply to no-return cases, where an assessment might be made at any time, is further evidenced by the proceedings at the hearings before the Committee on Finance of the Senate upon the Revenue Act of 1914, and from the discussion of that provision in the 1926 Act, when same was before the Senate.

This was made quite plain by Mr. A. W. Gregg, then General Counsel of the Bureau of Internal Revenue, at the hearings before the Committee on Finance of the Senate upon the Revenue Act of 1924, when considering the

effect of these provisions as they appeared in Section 1009 (b) and (c) of that Act, quoted, supra, and which are identical with Section 278 (a) and (d) of the same Act, and also as they appeared in Section 278. We set forth the substance of the proceedings as they appear on pp. 39, 40, 41, 49, 50, 51 and 52.

Section 278 (d) of the 1924 Revenue Bill, as it came to the Senate from the House, provided "Where the assessment of the tax is made within the period prescribed in Sec. 277 or in this section, such tax may be collected at any time by distraint or by proceeding in court * * *." In considering this sub-section a discussion arose between Mr. Gregg and various senators (pp. 39-41) as to whether or not there should be a time limit upon the right to collect after an assessment had been made and not leave the time within which the Government may collect open forever, by the use of the phrase "at any time." Action thereon was deferred, but several days later the Committee took up for consideration Section 1009 (b) and (c) of the bill, which was in identical language in that respect with Section 278 (a) and (d). In that discussion (pp. 49-52) several senators insisted that after the Government had made an assessment there should be a limit upon the time within which it might proceed to collect. Thereupon the question arose as to whether this should apply to fraud cases and no-return cases, when the following colloquy took place:

> "Senator King (interposing). You distinguish between cases where a return is filed and where there is no intent to deceive and cases where a man deliberately files no return?

"Mr. Gregg. Yes, sir.

"Senator King. In the first instance you were put on notice and you can inquire and ascertain whether there have been any omissions in the return. In the second instance you have not been put on notice, and your contention is that you should have an indefinite period within which to make your assessment. But do you not think in the latter case, after you have made the assessment, there ought to be a limitation within which you may prosecute to a successful issue your claim for the tax?

"Mr. Gregg. * * * There are cases occasionally where we find a taxpayer has failed to file a return, but sometimes we can not prove deliberate fraud. It seems to me that the statute should not begin to run against the Government until the Government is put on notice in a case of this kind.

"Senator Reed of Pennsylvania. The only offenses against which there are no statute of limitations are murder and treason. Why should we class this offense with those two?

"Mr. Gregg. This is not a penalty for the offense; this is for the collection of the tax. There is a statute of limitations on the criminal penalties.

"Senator Reed of Pennsylvania. This is not a thing that I would debate at any length.

* * * * *

"Senator King. As far as I am concerned, if they put in a provision that, after having made the assessment, there will be a period of limitation of 10 years within which they must prosecute to a successful conclusion—

"Senator Jones of New Mexico (interposing). I think six years would be all right.

"The Chairman. Turn to page 177 of the bill and let us fix both of them at the same time.

"Mr. Gregg. Page 177, line 15, strike out the words 'at any time' and insert 'within six years after the assessment.'"

This intention of Congress to put a limitation of six years upon proceedings for the collection of taxes assessed in those cases where no return had been filed, was again evidenced by the interpretation placed upon Section 278 (d) of the Revenue Act of 1926, when that subdivision was up for discussion before the Senate, after that section, as it appeared in the 1924 Act, had been rewritten by the Senate Finance Committee to make it retroactive, in the language in which it appeared in the 1926 Act as passed.

It has been heretofore shown that "fraudulent return" cases and "no return" cases are coupled together in the same limitation provisions of Section 278, consequently whatever limitation provisions applied to "fraud" cases would necessarily apply to "no-return" cases.

Section 278 (d) of the 1926 Act came up for discussion on the floor of the Senate on February 5th, 1926, after having been reported as rewritten by the Senate Finance Committee, when the following colloquy took place between Senator King of Utah and Senator Reed of Pennsylvania, ranking member of the Senate Finance Committee to the Chairman, and in charge of the bill on the floor of the Senate at the time:

"Mr. Reed of Pennsylvania. Now Mr. President, I ask consideration of the committee amendment at the bottom of page 137.

"The Vice President. The amendment will be stated.

"The Chief Clerk. On page 137, after line 23, the Committee on Finance proposes to strike out:

"(d) Where the assessment of the tax is made within the period prescribed in section 277 or in this section, such tax may be collected by distraint or by a proceeding in court, begun (1) within six years after the assessment of the tax, or (2) at any time prior to the expiration of any period for collection agreed upon in writing by the commissioner and the taxpayer.

"(e) This section shall not affect any assessment made, or distraint or proceeding in court begun, before the enactment of this act, nor shall it authorize the assessment of a tax or the collection thereof by distraint or by a proceeding in court (1) if at the time of the enactment of this act such assessment, distraint, or proceeding was barred by the period of limitation then in existence, or (2) contrary to the provisions of subdivision (a) of section 274.

"And in lieu thereof to insert:

"(d) Where the assessment of any income, excess-profits, or war-profits tax imposed by this title or by prior act of Congress has been made (whether before or after the enactment of this act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the commissioner and the taxpayer.

"(e) This section shall not bar a distraint or proceeding in court begun before the enactment of the revenue act of 1924; nor shall it authorize the assessment of a tax or the collection thereof by distraint or by proceeding in court (1) if at the time of the enactment of this act such assessment, distraint

or proceeding was barred by the statutory period of limitation properly applicable thereto, unless prior to the enactment of this act the commissioner and the taxpayer agreed in writing thereto, or (2) contrary to the provisions of subdivision (a) of section 274 of this act.

"Mr. King: That relates to fraud, does it not?

"Mr. Reed of Pensylvania: Yes.

"The Vice-President: The question is on agreeing to the amendment.

"The amendment was agreed to."

(Volume 67, No. 43, Congressional Record, 69th Congress, First Session dated Friday, February 5th, 1926, page 3,068).

The House of Representatives had the same understanding of the meaning of this section, because in describing the scope of Section 278 (d) in report No. 1 of the Committee on Ways and Means of the House of Representatives on House Roll No. 1, (Rev. Act of 1926) dated December 7, 1925, at page 12, it was said:

"Sub-division (d) provides that where an assessment of tax is made such tax may be collected by distraint or proceeding in court begun within six years of the assessment of the tax or at any time prior to the expiration of any period for collection agreed upon in writing by the commissioner and the taxpayer."

Later after the 1926 Act had passed the Senate and the bill had gone to conference, the Managers on the Part of the House, in making their report of the Conference Committee to the House, in Conference Report to the House of Representatives, No. 356, accepting House Roll

No. 1, dated February 22, 1926, said, on page 42, respecting certain amendments made to Section 278 (d) by the Senate:

> "This amendment rewrites in more definite language, and correcting clerical mistakes, subdivisions (d) and (e) of section 278 of the House bill, dealing with the time within which distraint or proceeding in court may be begun after the assessment has been made."

In the opinion of Honorable T. C. Munger, D. J., herein, 25 Fed. (2d) 746, (R. 68), respecting this feature of the case, it was said:

> "Whether the return was required to be made within three years or no limitation of time was imposed, the assessment was made in the statutory period of limitation applicable thereto."

In the opinion of the Circuit Court of Appeals, in this case (R. 395), in discussing this contention of the Government, it is said:

> "It is vigorously urged that in a no-return case there is no period of limitation for assessment, and therefore, this section does not apply. But the argument does not persuade. *The intent in the words 'within the statutory period of limitation applicable thereto' is too plain for mistake.* This section authorizes the Government to sue after a proper assessment; the Board of Tax Appeals had been created, and Congress wanted to extend the time for suit for a reasonable period after assessment, so that appeals to the board could be prosecuted, etc. But Congress didn't want to give that right to sue if the assessment was barred by the statute when it was made. Therefore Congress qualified the right to sue by providing that the assessment must have been made in time. The assessment here was made in

time, and that phrase has served its purpose." (Our italics)

In the *Florsheim Bros. Dry Goods Co. vs. United States,* (decided by this court February 24, 1930), it is said, respecting this Section in the 1926 Act:

"Section 278 (d) prescribed the period of limitation for the collection of taxes applicable to all cases enumerated in that Section."

II.

The Collection Of The Sum Sought To Be Recovered Herein From The Defendants, As Transferees Of The Assets Of The Updike Grain Company, Is Barred By Section 250 (d) Of The Revenue Act of 1921 And Section 277 Of The Revenue Act of 1924.

Omitting the inapplicable provisions, the above Sections are as follows:

Section 250 (d)—Revenue Act of 1921. (42 Stat. 265)

"The amount of income, excess profits, or war profits taxes * * due under any return made under this act for prior taxable years or under prior income, excess profits, or war profits tax acts, * * shall be determined and assessed within five years after the return was filed, * *; and no suit or proceeding for the collection of any such taxes due under this act or under prior income, excess profits, or war profits tax acts, * * shall be begun, after the expiration of five years after the date when such return was filed, * * *."

Section 277 (a) (2)—Revenue Act of 1924. (43 Stat. 299)

"The amount of income, excess profits, and war profits taxes imposed by * * the Revenue Act of 1917,

> * * and by any such act as amended, shall be assessed within five years after the return was filed, and no proceeding in court for the collection of such taxes shall be begun after the expiration of such period."

The above sections contain limitation provisions in cases where returns were filed and limit proceedings for the collection of the tax, where a return was filed, to five years after the filing of the return. If a return was filed within the meaning of these provisions, the right to collect this tax became barred in August, 1922, and the liability for the tax was extinguished by Section 1106 (a) of the Revenue Act of 1926.

It becomes necessary to ascertain if returns were filed for the Updike Grain Company in 1917, which started the running of the above limitation provisions.

The record shows that the taxpayer had duly "designated a fiscal year for the computation of its tax" pursuant to Section 13 (b) of the Revenue Act of 1916 (39 Stat. 771), and Section 200 of the Revenue Act of 1917 (40 Stat. 302) (see appendix), which ended June 30, 1917 (R. 161).

Both the 1916 Act (Sec. 13 (b)) and the 1917 Act (Sec. 212) (40 Stat. 307) (See appendix) required the taxpayer to "render" "within sixty days after the close of such fiscal year" "a true and accurate return of its annual net income in the manner and form prescribed by the Commissioner of Internal Revenue * * * and containing such facts, data, and information as are appropriate and in the opinion of the Commissioner necessary to determine the correctness of the net income returned

and to carry out the provisions of "Title I (the 2% tax prescribed in Sec. 10) or suffer a penalty of 50% of the tax (Sec. 3176 R. S. as amended by Sec. 16, Revenue Act of 1916).

Both the 1916 Act (Sec. 14 (a)) and the 1917 Act (Secs. 4 and 212) (See appendix) required the taxpayer to pay the tax due upon such return on or before December, 1917, or suffer a 5% penalty and interest at 1% per month thereafter from due date.

The taxpayer filed its returns within sixty days after the close of its fiscal year (R. 165, 171, 175) exactly as required by the Revenue Acts of 1916 and 1917, and paid the tax due within 105 days thereafter or before December, 1917, as was also required by both Acts.

The 1917 Act made no other requirements of the taxpayer respecting the filing of its returns or the time of paying its tax.

The Commissioner on January 2, 1918, after the period fixed by law, within which the taxpayer was required to file its returns, had expired, promulgated regulation 33 (Rev.) Art. 61, providing that:

> "A corporation which was dissolved in 1917, prior to passage of war revenue Act of October 3, 1917, is subject to tax under the Act of September 8, 1916, as amended, and also to the war income tax and the war excess profits tax imposed by the Act of October 3, 1917. (*Brady, et al. v. Anderson,* 240 Fed. 665). Corporations so situated will make a return on revised Form 1031, covering the period in 1917 during which it was in business prior to its dissolution. If it shall have previously made a re-

turn covering this period and shall have paid any excess profits tax under the Act of March 5, 1917, it shall be entitled to credit for the amount of such tax so paid against any excess profits tax assessable against it under Title II of the Act of October 3, 1917."

The regulation did not say when such return should be filed, by corporations which had made returns during the year 1917, for a fiscal year ending during that year, and there was no law (other than above stated) or regulation which fixed the time, although there was respecting corporations making returns upon a calendar year basis. Neither did the regulation provide who should sign the returns of a dissolved corporation, nor which "revised Form 1031" was meant. The only one known to taxpayers then was Form 1031 (Revised 1916) which was presumably meant, and upon which form the taxpayer had already made its returns.

Although the law and regulations, existing at the time the taxpayer made its returns and at the time this regulation was promulgated, required two returns, one on Form 1031, revised 1916, termed "Income Tax Return" and another on Form 1103, termed "Excess-Profits Tax Return", the regulation, you will note, did not require the filing of an additional Excess Profits Tax Return on Form 1103, or any other form.

The return made by the taxpayer on revised Form 1031, in August, 1917, was a true and accurate return of its net income in the manner and form then prescribed by the Commissioner of Internal Revenue, and was declared to be such by the Revenue Agent, who by

authority of the Commissioner and Regulation 33, Article 186 (See appendix) made a field audit of same, and of the returns of the taxpayer for several previous years, in October, 1918, because in his report on this audit, he said:

> "From all books and records available, it appeared that the full amount of gross income for each year was reported and no improper deductions taken." (R. 107).

The undisputed record shows the following:

(a) The returns as filed by the Updike Grain Company set forth specifically the gross amount of income from all separate sources of said company for the year 1917 and for the eleven month period ending June 30th, 1917, and the aggregate items of allowance claimed by the company and authorized by law, and the total and entire net income and earnings of the company for such eleven month period and for the periods January 1, 1917, to June 30, 1917, and July 1, 1917, to the date of dissolution of the company in August, 1917, and all other facts, data and information appropriate and necessary to determine the net income and to carry out any applicable provisions of the Revenue Act of October 3, 1917. (R. 165, 171, 175).

(b) No notice, demanding additional returns, was sent to the company as required by Regulation 33, Article 196, supra. (R. 95, 349, 350).

(c) When the Commissioner requested the Revenue Agent in Charge at Omaha to make an audit of the books and records of the company to ascertain the amount of additional tax due, he requested him to audit the 1917 returns of the company which had been filed, and did not claim or advise that no return had been filed. (R. 95).

(d) The Revenue Agent making the audit for the year 1917 asked for, received and used the copies

of the returns filed by the company for that year in making his examination and audit. (R. 350).

(e) The Revenue Agent in Charge and the Revenue Agent making the examination proceeded upon the theory that a return had been made, which their correspondence clearly indicates. (R. 107, 117, 121, 105, 317, 323, 325, 335).

(f) In the report of the Revenue Agent making the examination, he refers to the computations for the year in question as an "*amended return*", which designation was apparently accepted by the Commissioner, because it was upon the figures thus set forth that the Commissioner determined and assessed the tax. (R. 107).

(g) The Revenue Agent making the audit of the returns filed by the taxpayer said in his report:

> "From all books and records available, it appeared that the full amount of gross income for each year was reported and no improper deduction taken." (R. 107).

(h) The Revenue Agent, making the examination and audit of the 1917 returns, prepared "a return" for the Commissioner pursuant to Sec. 14 (a), Revenue Act of 1916, both for the War Income and Excess Profits Tax under the October 3, 1917 Act. (R. 115).

(i) No penalty was assessed against the company for failure to file a return, which it was the duty of the Commissioner under the regulations and law to assess where no return had been filed, and had he not been accepting the returns filed as sufficient. (Sec. 1004, Rev. Act, 1917; Reg. 33, Art. 21; Reg. 33, Art. 197; Reg. 33, (Rev.) Art. 214, para. 629). (R. 148) (See Appendix for Statute and Regulations)

(j) In a letter dated April 27, 1923, from the Collector of Internal Revenue, Omaha, Nebraska, to

the Commissioner of Internal Revenue, attention is called to this tax, and in that letter it is stated:

> "It is claimed by the taxpayers that they made returns for the part of the year 1917 up to the time of the dissolution." (R. 225).

(k) The Solicitor of Internal Revenue in his opinion of May 4th, 1923, recognized the fact that returns had been filed for the period in question. (R. 233).

(l) The Bureau of Internal Revenue and the Department of Justice, in the suit brought against Mr. Updike to recover the taxes assessed against the Missouri Valley Elevator Company, recognized that the returns filed by that company, which were of like character to the returns filed for the Updike Grain Company, were sufficient returns to start the running of the statute of limitations in cases where returns had been filed, had they not charged them to be "incorrect, misleading and false in law." (R. 361).

It appears from the foregoing that the returns filed by the company were recognized as sufficient under the October, 1917, Act, (1) by the Collector of Internal Revenue at Omaha; (2) by the Commissioner of Internal Revenue, in directing a revenue agent to make the investigation, who was empowered to do so only in cases where returns were made; (Reg. 33, Art. 186; Treas. Dec. 1932, para. 5; Reg. 33 (Rev.) Art. 221, para. 639; Reg. 45, Art. 1012) (See appendix) (3) by the Revenue Agent in Charge at Omaha; (4) by the Revenue Agent making the investigation and audit; (5) by the Solicitor for the Bureau of Internal Revenue; (6) by the Proving and Audit Divisions in endorsing the additional assessment on the return; and (7) by the Commissioner of Internal Revenue

in making the assessment, as so endorsed; and (8) by the Department of Justice in the Missouri Valley Elevator Company case.

As a result of the foregoing the taxpayer, and likewise the former officers and stockholders, had the right to assume, and at all times did assume, that the returns as filed were sufficient. By the conduct of the various governmental officers recited above, the taxpayer and the stockholders and transferees were lured and lulled into the belief and security that the company had complied with all the rules, regulations and laws respecting returns, for its income for the year 1917, and had thereby escaped any penalties or disadvantages imposed upon one not filing returns.

Tucker vs. Alexander, 275 U. S. 228.

Zeller vs. United States, 35 Fed. (2d) 870.

Ritter vs. United States, 28 Fed. (2d) 265.

Union Trust Company vs. McCaughn, 24 Fed. (2d) 459.

If it should be held that the returns filed by the taxpayer were not sufficient to start the running of the limitation provisions in Sections 250 (d) and 277, quoted above, then we contend that the returns prepared by the Commissioner of Internal Revenue, through the Revenue Agent and the Revenue Agent in Charge in Omaha, in October, 1918, and forwarded to the Commissioner of Internal Revenue by the Revenue Agent in Charge, under date of October 26th, 1918, was "a return" within the meaning of Section 278 (a) of the 1924 and 1926 Acts,

(See appendix) as was held in the opinion of the District Court by Honorable T. C. Munger, D. J. (R. 68), pursuant to the authority of the following provisions of the Revenue Act of 1916, and the regulations cited:

Section 14 (a) of the Revenue Act of 1916 (39 Stat. 772):

> " * * * That every corporation, * * * computing taxes upon the income of the fiscal year which it may designate in the manner hereinbefore provided, shall pay the taxes due under its assessment within one hundred and five days after the date upon which it is required to file its list or return of income for assessment; except in cases of refusal or neglect to make such return, * * * in which cases the Commissioner of Internal Revenue shall, upon the discovery thereof, at any time within three years after said return is due, make a return upon information obtained as provided for in this title or by existing law; * * * *Provided,* That upon the examination of any return of income made pursuant to this title, * * * if it shall appear that amounts of tax have been paid in excess of those properly due, the taxpayer shall be permitted to present a claim for refund thereof notwithstanding the provisions of section thirty-two hundred and twenty-eight of the Revised Statutes;"

Section 14 (b) of the Revenue Act of 1916 (39 Stat. 772):

> "When the assessment shall be made, as provided in this title, the returns, together with any corrections thereof which may have been made by the commissioner, shall be filed in the office of the Commissioner of Internal Revenue * * * "

The same authority to the Commissioner to make returns is found in various regulations in force at the time

the Commissioner made returns in the instant case, particularly in the following:

Regulation 33, Article 177.

Regulation 33, Article 184.

Regulation 33 (Revised), Article 42, Paragraph 253.

If it be claimed that this case does not come within the provisions of Section 277 or Section 278 of the Revenue Act of 1926, then it must be governed by Section 1109 (a) (1), (2) and (3), (44 Stat. 114), which is the dragnet limitation section intended to cover all cases for which there is no specific provision. The sub-divisions of this section are as follows:

"(a) Except as provided in sections 277, 278, 310 and 311—

"(1) Notwithstanding the provisions of section 3182 of the Revised Statutes or any other provision of law, all internal-revenue taxes shall (except as provided in paragraph (2) or (3) of this subdivision) be assessed within four years after such taxes became due, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of five years after such taxes became due.

"(2) In case of a false or fraudulent return with intent to evade tax, of a failure to file a return within the time required by law, or of a willful attempt in any manner to defeat or evade tax, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment at any time.

"(3) Where the assessment of any tax imposed by this Act or by prior Act of Congress has been

made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (A) within six years after the assessment of the tax, or (B) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer."

III.

If The Collection Of These Taxes From The Updike Grain Company, At The Time These Proceedings Were Begun, Is Barred By The Limitations Contained In Any Of The Revenue Acts, This Suit Cannot Be Maintained Against The Transferees As An Independent Suit For The Recovery Of Trust Funds.

The attempted application by the Government of the "trust fund theory" to this case, will not authorize the prosecution of the suit, if it is determined by the court that a suit against the taxpayer would have been barred by the provisions of Sec. 278 (d) of the Revenue Act of 1926, or by any earlier provisions of the revenue law, for the reason that the trust fund theory, in the form propounded by the Government in its argument, has been expressly repudiated by this court in *Graham vs. Railroad Co.*, 102 U. S. 148; *Fogg v. Blair*, 133 U. S. 534; *Hollins v. Brierfield Coal & Iron Co.*, 150 U. S. 371; *McDonald v. Williams*, 174 U. S. 397; *Pierce v. United States*, 255 U. S. 398, and by state decisions in *Shaw v. Robinson & Stokes*. 50 Neb. 403; *Coleman v. Hagey*, 252 Mo. 102; *Leudecke v. Des Moines Co.*, 140 Ia. 223, and *Hospes v. N. W. Mfg. Co.*, 48 Minn. 174, as well as in numerous other decisions. It does not apply to this case in any event, because the primary question here is not

the application of a statute of limitations to the suit against the transferees, but to the absence, in complainant's case, of a fundamental prerequisite for the prosecution of a suit against the transferee, to-wit, the existence of a present enforceable claim against the transferor. But, in any case, a suit against the transferee is a proceeding in court for the collection of a tax within the meaning of Sec. 278 (d), as appears from the Government's petition in this case (R. 8), even after it had been amended for the purpose of converting it into a general equity suit (R. 12-155, 6, 7-160), because it is based upon the averment that the tax accrued against the taxpayer, and that the property in the hands of the transferees is liable to the payment of that tax, and the prayer is that the amount of the tax be recovered. As such a suit is, in its essence, a creditor's bill, it is ancillary to the claim upon which it is based, and a part of the proceedings for the collection of the tax. A creditor's bill has been called an equitable execution, and whether it is invoked in aid of the collection of a judgment at law, where execution fails, or in aid of the collection of a tax against the transferor, if such a suit is permissible without a judgment at law, it remains essentially an ancillary proceeding, which, in no case, can rise higher than its source, or be enforceable after the claim upon which it is founded ceases to be enforceable against the transferor. *Merchants Nat. Bk. vs. McDonald,* 63 Neb. 363; *Pierce vs. United States,* 255 U. S. 398; *Dole vs. Wilson,* 39 Minn. 330; *Flagg vs. Flagg,* 39 Neb. 229; *Holmes v. Webster,* 98 Neb. 105; *Fisher v. Woodard,* 103 Neb. 253; *Newell v. Dart,* 28 Minn. 243; *Scott v. Neely,* 140 U. S. 106; *Bank v. Braithwaite,* 7 N. Dak. 352; *Mc-*

Aleer v. Clay Co., 42 Fed. 665; *Board v. Tome*, 153 Fed. 81; *Gen. Elec. v. Hurd*, 171 Fed. 984; *Mullen v. Hewitt*, 103 Mo. 639.

IV.

The Assets Of The Updike Grain Company Were Transferred To The Respondents Herein In August, 1917; The Liability For The Tax Did Not Arise In Any Event Until The Passage Of The Revenue Act of 1917, On October 3, 1917, And This Suit Against Such Transferees Cannot Be Maintained, Because The Government Thereby, If At All, Became A Creditor For Such Tax Subsequent To The Time The Transferees Received The Assets, There Being At The Time Of Transfer No Tax Liability Nor An Existing Statute Under Which A Tax Liability Could Arise.

No claim is made against the respondents solely because they are stockholders of the corporate taxpayer, it is not claimed that there is any statute of the State of Nebraska, where the corporation is organized, that makes them liable, and there is no statute of the United States which makes them liable as stockholders, or as transferees of the corporate assets; not even Sec. 280 attempts either to create or enlarge the liability of transferees of assets, but merely regulates a procedure for enforcing by summary process whatever existing liability there may be at law or equity. Necessarily, therefore, whatever liability exists is that which grows out of the laws of Nebraska, including such general rules of law as are construed and defined in the courts of the United States with reference to transactions arising under the laws of the State of Nebraska. The liability to creditors growing out of the transfer of assets of a corporation to its stockholders is, in a proceeding of this character, precisely the same as the liability of the transferee of assets of an individual. (*Graham v. Railroad Co.*, 102 U. S. 148;

Hollins v. Brierfield, 150 U. S. 371; *Pierce v. United States,* 255 U. S. 398). It is only when a court of equity has taken over the liquidation of a corporation, that there is any trust which differs from the status of the transferred assets of an individual debtor and the claims of the creditors. In each case the right of the creditor to pursue the assets is a remedy granted to the creditor because of the inadequacy of legal remedies, either because a judgment at law and the failure of execution has demonstrated the insufficiency of the legal remedies, or because a court of equity, in administering the remedy directly, without a prior judgment at law, has become satisfied that there is no remedy in the proceedings at law, and that the remedies in equity are therefore available. But it is universally held in the decisions defining and enforcing this equitable remedy, that it is available only to a creditor existing at the time of the transfer. This is true whether the transfer was fraudulent as against existing creditors, or whether it was only voluntary, and therefore capable of being set aside by existing creditors. But in no case is the remedy available to a subsequent creditor, unless, in some jurisdictions he can allege and prove that the transfer was made in contemplation of a debt to be contracted and was intended as a fraud upon such creditor. In this case there is no allegation of any intention on the part of the corporation or its stockholders to defraud the Government by distributing its assets and dissolving in August, 1917, but, on the contrary, the averment is that the dissolution was "duly" made (R. 9), that the resolution of the stockholders providing for dissolution of the corporation and the transfer of its assets was "duly" adopted by the

stockholders, and that thereafter (R. 10) legal steps to complete the dissolution were "duly" taken. Of course the meaning of the word "duly" is that the steps were lawfully taken, (Century Dictionary, Standard Dictionary, 19 C. J. 833, *State Bank v. Morse*, 60 Kas. 526; *Robertson, Col. v. Perkins*, 129 U. S. 333) and it is no where alleged that they were taken unlawfully and for the purpose of defrauding the Government, nor is there any proof whatever to that effect. The averment in the Government's petition that the action of the corporation was "duly" taken, applies as well to the resolution directing the distribution of the assets among the stockholders, as to the technical steps relating to the dissolution itself.

The right to pursue the assets of a debtor to satisfy the claims of a creditor, as distinguished from the procedure, is based upon Statute 13, Eliz. c5, and the various statutes of the states re-enacting that statute, with modifications or enlargements. (*Sexton v. Wheaton*, 8 Wheat. 229; *Mattingly v. Nye*, 8 Wall. 370; *Graham v. Railroad Co.*, 102 U. S. 148; *Hollins v. Brierfield*, 150 U. S. 371; *Shaw v. Robinson & Stokes*, 50 Neb. 403; *Hospes* v. *N. W. Mfg. Co.*, 48 Minn. 174). And under these decisions, the right of the creditor is grounded upon the statute, and applies alike to the creditors of an individual and the creditors of a corporation.

If the action against the taxpayer was barred by Sec. 278 (d) of the Revenue Act of 1926, then the Government cannot succeed in this proceeding, because it lacks an essential element in its case, that is, a debt existing at the time of the suit, and whether barred by that sec-

tion or not, the Government cannot recover against the stockholders, because it is a subsequent creditor, and not in a position to attack a bona fide transfer completed before the Government's claim was even authorized by a statute.

While it is true that the decisions of various district courts and circuit courts of appeal are to the effect that a corporation lawfully (that is "duly") dissolved in 1917, prior to the passage of the act of October 3, 1917, is liable to the increased tax imposed by that act, yet this court has no where so decided, and its refusal to grant a certiorari in the first case of *Updike v. United States*, 8 Fed. (2nd) 913, 271 U. S. 661, does not imply any approval by this court of the decisions of the district or circuit court in that case, and certainly not in any of the other cases which did not reach this court. (*United States vs. Carver*, 260 U. S. 482).

V.

The Provisions Of The Revenue Act Of October 3, 1917, Are Not Applicable To A Corporation Which Was Lawfully Dissolved Under State Law, After Having Discharged All Its Existing Obligations And Distributed All Its Assets Among Its Stockholders, Prior To The Enactment Of The Suit.

In accordance with the first ruling made by the Commissioner of Internal Revenue in October, 1917, after the passage of the act (R. 187), the stockholders of the Updike Grain Company have contended that the act of October 3, 1917, was not applicable to a corporation which was dissolved before the act was passed, because, whether it was in the power of Congress or not, no intention was shown in that act to revive a dissolved corporation

for the purpose of taxing it. By the final section of the act, 40 Statutes at Large, 338, §1302, it was provided that, unless as otherwise provided in the act, it should take effect and be in force on the day after its passage, and as it was passed on October 3, 1917, it took effect and became in force on October 4, 1917. So far as affects this controversy, the only feature of the act which could be called retroactive, are the provisions of Sections 4 and 200 of the act, (40 St. at L. 302) to the effect that the first taxable year under the act should be the year 1917, and that for corporations having a fiscal year, the first taxable year should be the fiscal year ending during 1917. That Congress thereby declared an intention of applying the terms of the act to all incomes during any part of the calendar year 1917, is conceded, but the contention of the stockholders at all times has been that the statute no where evinced an intention of taxing corporations which had passed out of existence, nor the transferees or stockholders of such corporations, conceding to the fullest extent the power of Congress to do so, if it had indicated its intention to take such action. The income tax is a personal tax; it is in no sense a levy upon specific property. All the provisions of the law indicate that it creates a personal liability on the part of persons and corporations, and its failure to specify that its terms are applicable to the stockholders of dissolved corporations, under the familiar rule that a tax statute will not be extended by implication, means that a tax was not assessable on account of income received by a then defunct corporation. *Smietanka v. Trust & Savings Bank,* 257 U. S. 602; *Schwab v. Doyle,* 258 U. S. 529; *Union Trust Co. v. Wardell,* 258 U. S. 537; *Gould v. Gould,* 245 U. S. 151,

Anderson v. Railway Co., 216 Fed. 83 (C. C. A. 2d Circuit), (Excise Tax of 1909); *Scott v. Railway Co.*, 246 Fed. 545 (C. C. A. 9th Circuit); *Pa. Steel Co. v. Railway Co.*, 198 Fed. 774 (C. C. A. 2d Circuit).

For the foregoing reasons we submit that the decrees and judgments of the District Court and the Circuit Court of Appeals, herein, are correct and should be affirmed.

Respectfully submitted,

WARREN H. HOWARD,

FRANCIS A. BROGAN,

ALFRED G. ELLICK,

Solicitors for Respondent,
GEORGE A. ROBERTS.

APPENDIX

Revenue Act of 1916

Section 13 (b) Revenue Act of 1916 (39 Stat. 771):

"(b). Every corporation, joint-stock company or association, or insurance company, subject to the tax herein imposed, shall, on or before the first day of March, nineteen hundred and seventeen, and the first day of March in each year thereafter, or, if it has designated a fiscal year for the computation of its tax, then within sixty days after the close of such fiscal year ending prior to December thirty-first, nineteen hundred and sixteen, and the close of each such fiscal year thereafter, render a true and accurate return of its annual net income in the manner and form to be prescribed by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, and containing such facts, data, and information as are appropriate and in the opinion of the commissioner necessary to determine the correctness of the net income returned and to carry out the provisions of this title. The return shall be sworn to by the president, vice-president, or other principal officer, and by the treasurer or assistant treasurer. The return shall be made to the collector of the district in which is located the principal office of the corporation, company, or association, where are kept its books of account and other data from which the return is prepared, or in the case of a foreign corporation, company, or association, to the collector of the district in which is located its principal place of business in the United States, or if it have no principal place of business, office, or agency in the United States, then to the collector of internal revenue at Baltimore, Maryland. All such returns shall as received be transmitted forthwith by the collector to the Commissioner of Internal Revenue."

Revenue Act of 1917

Section 4, Revenue Act of 1917 (40 Stat. 302):

"That in addition to the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, there shall be levied, assessed, collected, and paid a like tax of four percentum upon the income received in the calendar year nineteen hundred and seventeen and every calendar year thereafter, by every corporation, joint-stock company or association, or insurance company, subject to the tax imposed by that subdivision of that section, except that if it has fixed its own fiscal year, the tax imposed by this section for the fiscal year ending during the calendar year nineteen hundred and seventeen shall be levied, assessed, collected, and paid only on that proportion of its income for such fiscal year which the period between January first, nineteen hundred and seventeen, and the end of such fiscal year bears to the whole of such fiscal year.

"The tax imposed by this section shall be computed, levied, assessed, collected, and paid upon the same incomes and in the same manner as the tax imposed by subdivision (a) of section ten of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, except that for the purpose of the tax imposed by this section the income embraced in a return of a corporation, joint-stock company or association, or insurance company, shall be credited with the amount received as dividends upon the stock or from the net earnings of any other corporation, joint-stock company or association, or insurance company, which is taxable upon its net income as provided in this title."

Section 200, Revenue Act of 1917 (40 Stat. 302):

"That when used in this title—

* * * * *

The term 'taxable year' means the twelve months ending December thirty-first, excepting in the case of

a corporation or partnership which has fixed its own fiscal year, in which case it means such fiscal year. The first taxable year shall be the year ending December thirty-first, nineteen hundred and seventeen, except that in the case of a corporation or partnership which has fixed its own fiscal year, it shall be the fiscal year ending during the calendar year nineteen hundred and seventeen. If a corporation or partnership, prior to March first, nineteen hundred and eighteen, makes a return covering its own fiscal year, and includes therein the income received during that part of the fiscal year falling within the calendar year nineteen hundred and sixteen, the tax for such taxable year shall be that proportion of the tax computed upon the net income during such full fiscal year which the time from January first, nineteen hundred and seventeen, to the end of such fiscal year bears to the full fiscal year; * * *."

Section 212, Revenue Act of 1917 (40 Stat. 307):

"That all administrative, special, and general provisions of law, including the laws in relation to the assessment, remission, collection, and refund of internal-revenue taxes not heretofore specifically repealed, and not inconsistent with the provisions of this title are hereby extended and made applicable to all the provisions of this title and to the tax herein imposed, and all provisions of Title I of such Act of September eighth, nineteen hundred and sixteen, as amended by this Act, relating to returns and payment of the tax therein imposed, including penalties, are hereby made applicable to the tax imposed by this Title."

Section 1004, Revenue Act of 1917, (40 Stat. 325):

"That whoever fails to make any return required by this Act or the regulations made under authority thereof within the time prescribed or who makes any false or fraudulent return, and whoever evades or attempts to evade any tax imposed by this

Act or fails to collect or truly to account for and pay over any such tax, shall be subject to a penalty of not more than $1,000, or to imprisonment for not more than one year, or both, at the discretion of the court, and in addition thereto a penalty of double the tax evaded, or not collected, or accounted for and paid over, to be assessed and collected in the same manner as taxes are assessed and collected, in any case in which the punishment is not otherwise specifically provided."

—o—

Revenue Act of 1924

Section 278 (a) (d) (e), Revenue Act of 1924 (43 Stat. 299):

"(a) In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

"(d) Where the assessment of the tax is made within the period prescribed in section 277 or in this section, such tax may be collected by distraint or by a proceeding in court, begun within six years after the assessment of the tax. Nothing in this Act shall be construed as preventing the beginning, without assessment, of a proceeding in court for the collection of the tax at any time before the expiration of the period within which an assessment may be made."

"(e) This section shall not (1) authorize the assessment of a tax or the collection thereof by distraint or by a proceeding in court if at the time of the enactment of this Act such assessment, distraint, or proceeding was barred by the period of limitation then in existence, or (2) affect any assessment made, or distraint or proceeding in court begun, before the enactment of this Act."

—o—

Revenue Act of 1926

Section 277 (a) (1) (2) (3) (4), Revenue Act of 1926 (44 Stat. 58):

"(a) Except as provided in section 278—

"(1) The amount of income taxes imposed by this Act shall be assessed within three years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period."

"(2) The amount of income, excess-profits, and war-profits taxes imposed by the Revenue Act of 1921, and by such Act as amended, for the taxable year 1921 and succeeding taxable years, and the amount of income taxes imposed by the Revenue Act of 1924, shall be assessed within four years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period."

"(3) The amount of income, excess-profits, and war-profits taxes imposed by the Act entitled 'An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes,' approved August 5, 1909, the Act entitled 'An Act to reduce tariff duties and to provide revenue for the Government and for other purposes,' approved October 3, 1913, the Revenue Act of 1916, the Revenue Act of 1917, the Revenue Act of 1918, and by any such Act as amended, shall be assessed within five years after the return was filed, and no proceeding in court without assessment for the collection of such taxes shall be begun after the expiration of such period."

" (4) In the case of income received during the lifetime of a decedent, the tax shall be assessed, and any proceeding in court without assessment for the collection of such tax shall be begun, within one

year after written request therefor (filed after the return is made) by the executor, administrator, or the fiduciary representing the estate of such decedent, but not after the expiration of the period prescribed for the assessment of the tax in paragraph (1), (2), or (3) of this subdivision."

Section 278 (a) (d) (e), Revenue Act of 1926 (44 Stat. 59):

"(a) In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

"(d) Where the assessment of any income, excess-profits, or war-profits tax imposed by this title or by prior Act of Congress has been made (whether before or after the enactment of this Act) within the statutory period of limitation properly applicable thereto, such tax may be collected by distraint or by a proceeding in court (begun before or after the enactment of this Act), but only if begun (1) within six years after the assessment of the tax, or (2) prior to the expiration of any period for collection agreed upon in writing by the Commissioner and the taxpayer."

"(e) This section shall not bar a distraint or proceeding in court begun before the enactment of the Revenue Act of 1924; nor shall it authorize the assessment of a tax or the collection thereof by distraint or by proceeding in court (1) if at the time of the enactment of this Act such assessment, distraint or proceeding was barred by the statutory period of limitation properly applicable thereto, unless prior to the enactment of this Act the Commissioner and the taxpayer agreed in writing thereto, or (2) contrary to the provisions of subdivision (a) of section 274 of this Act."

Section 280 (a) (1) (b) (1) (2), Revenue Act of 1926 (44 Stat. 61):

"(a) The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this title (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

"(1) The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this title or by any prior income, excess-profits, or war-profits tax Act."

"(b) The period of limitation for assessment of any such liability of a transferee or fiduciary shall be as follows:

"(1) Within one year after the expiration of the period of limitation for assessment against the taxpayer; or

"(2) If the period of limitation for assessment against the taxpayer expired before the enactment of this Act but assessment against the taxpayer was made within such period,—then within six years after the making of such assessment against the taxpayer, but in no case later than one year after the enactment of this Act."

Section 311 (a), Revenue Act of 1926. (44 Stat. 77):

"(a) In the case of a false or fraudulent return with intent to evade tax or of a failure to file a return the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

Section 1109 (a) (2), Revenue Act of 1926 (44 Stat. 114):

"(a) Except as provided in sections 277, 278, 310, and 311—

"(2) In case of a false or fraudulent return with intent to evade tax, of a failure to file a return within the time required by law, or of a willful attempt in any manner to defeat or evade tax, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

—o—

Regulations

Reg. 33, Art. 21:

"In case any perso liable to make return shall neglect or refuse to make or render a list or return, or shall render a willfully false or fraudulent return, it shall be the duty of the collector, after due notice has been given, to make such list, according to the best information he can obtain by the examination of such person, or any other evidence.

"When duly certified by the collector, the said list thus prepared shall be the return of said person and the tax so ascertained to be due, together with 50 per cent or 100 per cent penalty incurred, shall be assessed and collected."

Reg. 33, Art. 186:

"For the purpose of verifying any return, made pursuant to this act, the Commissioner of Internal Revenue may, by any duly authorized revenue agent or deputy collector, cause the books of such corporation to be examined, and if such examination discloses that the corporation is liable to tax in addi-

tion to that previously assessed, or assessable, the same shall be assessed and shall be payable immediately upon notice and demand. For the purpose of such examination, the books of corporations shall be open to the examining officer, or shall be produced for this purpose upon summons issued by any properly authorized officer."

Reg. 33, Art. 196:

"Where the required returns are not filed within the prescribed time, either by individuals or corporations, notice on Form 1045 should in each case be sent to the delinquent."

Reg. 33, Art. 197:

"When assessment has been made, collectors will, on receipt of their returned lists, at once issue preliminary notices of assessment (Form 647), and where in any case the tax assessed is not paid on or before the 30th day of June, or in case of corporations designating their own fiscal year, within 120 days following the date on which the return should have been filed, notice and demand (Form 17) should be at once issued, and unless the tax in such case is paid within 10 days after the service of such notice, general demand for tax, penalty, and interest (Form 21) should at once be issued. Immediate notice and demand (Form 17) will, however, be served in case of failure to file the required return within the statutory period."

Reg. 33 (Rev.), Art. 214, Para. 629:

"When a corporation has, in the manner provided by law, established a fiscal year other than the calendar year as the basis for making its return, it is bound by such action to make its returns on such basis until such fiscal year be properly changed. Failing to make its returns on the basis designated and

within the prescribed time will subject the corporation to the penalties imposed by this title for delinquency." (T. D. 2001, 2029, 2090, 2137).

Reg. 33 (Rev.), Art. 221, Para. 639:

"For the purpose of verifying the accuracy of a return, or for making one where none is made, the books of corporations and all other relative data shall be open to the inspection of the Commissioner of Internal Revenue or his duly authorized agents."

Reg. 45, Art. 1012:

"When the returns are received at the collectors' offices, they are examined and listed before being forwarded to the Commissioner. If it appears that the tax is greater or less than shown in the return, it is recomputed. After checking the figures the Commissioner assesses the tax on the basis of the collectors' lists. The collectors then send out bills for the taxes, either as computed by the taxpayer or as recomputed. If a taxpayer believes that he has been overassessed, he may file a claim for abatement or (after payment of the tax) for a refund of the excess. See section 252 of the statute and articles 1031-1038. As soon as practicable the returns are carefully audited by accountants in the office of the Commissioner at Washington, assisted where necessary by reports of the examination of taxpayers' books and records made by revenue agents in the field. If error in a return is detected, the taxpayer is notified accordingly and an additional assessment is made against him or he is given the opportunity to file a claim for a refund, as the case may be. Any assessment must be made within five years after the return was due or was made, except in the case of false or fraudulent returns with intent to evade the tax. See sections 228, 1305 and 1310 of the statute and articles 451 and 1711."

Regulations 33 were issued January 5, 1914.

Regulations 33 (Rev.) were issued January 2, 1918.

Regulations 45 were issued April 17, 1919.